SUMMARY OF ARGUMENT

Staff notes that this attachment is a summary of Staff's arguments, rather than a part thereof, and to the extent that any statement or representation in this Attachment A conflicts with any assertion that Staff advanced either in its testimony or briefs, the latter govern. Staff specifically reserves all the arguments made in its testimony and briefs, and the failure to specifically include some such argument or part thereof in this attachment should not be deemed a waiver of such argument.

I. Introduction/Summary of Position

Staff is convinced that SBC's retail business NAL is subject to imputation; that the UNE loop is a noncompetitive service or service element used to provide a competitive service within the meaning of Section 13-505.1 of the Public Utilities Act, such that SBC's retail business NAL must satisfy imputation based upon the TELRIC rate it charges for the UNE loop. Staff is further convinced that a "narrow" imputation test is the only lawful and proper test to use, and that revenues from usage and vertical services cannot and should not be included. Staff contends that SBC's retail business NAL rates do not pass imputation under a properly constructed test. Staff notes that there a number of rate design options that SBC can use to deal with this problem, but the Commission is under no obligation to give SBC direction or guidance in this regard. Finally, the Staff argues that Section 276 does not preempt the application of the imputation test to COPTS rates, and those rates can be altered consistent with both Section 276 and imputation, based on the methodology established by the Commission in its *Payphone Order*.

In its Reply Brief, the Staff pointed out that its positions and recommendations on imputation issues in this proceeding are conservative and entirely consistent with the Commission's resolution of similar issues in past imputation proceedings. *See* Staff RB at 2. The Staff recommended that the Commission resolve imputation issues in this proceeding in a like manner as it has resolved similar issues in past imputation proceedings, and seeks only to preserve the status quo in its competitive business NAL markets. Id.

The Staff noted that the positions of SBC and CUB, on the other hand, urge the Commission to embark upon a more adventurous course. As the first line of defense of their novel positions, SBC and CUB argue that no imputation test is needed as a result of the UNE loop rate increases in ICC Docket 02-0864. In order to make such a showing, SBC and CUB argue that UNEs are not "services" or "service elements" under Section 13-505.1 and, thus, there is no need for UNEs to be imputed to retail rates. SBC IB at 3; CUB IB at 4. As a second line of defense, SBC and CUB argue that business network access lines ("NALs") should not be treated as a stand-alone service under Section 13-505.1. SBC and CUB argue that the "service" should be defined to include the business NAL *plus* other products that *may* accompany the NAL, such as usage and features. Staff RB at 2-3.

Staff also noted that if the Commission does not accept their threshold argument that imputation is not needed, which position Staff demonstrates warrants rejection, SBC and CUB insist that whatever imputation test is required, it should not hinder their pricing flexibility. In order for the Commission to adopt their positions, SBC and CUB propose that the Commission disregard Section 13-505.1's plain language and legislative purpose, and abandon its past precedent requiring that *each* stand-alone service pass imputation and, instead, adopt a self-described "broad" imputation test. The Staff pointed out that the Commission has never adopted such a novel broad test before. In the Staff's view, moreover, the SBC and CUB proposal is far *too* broad. SBC's and CUB's broad imputation test scenarios would aggregate revenue, among other things, from disparate revenue streams in order for SBC's business NAL to pass imputation. Staff views SBC's and CUB's proposed broad test scenarios as inappropriate as they would certainly eviscerate the imputation protections contained in both the PUA and in the Commission's rules against price squeezes in certain Illinois telecommunication markets. The Staff recommends that the Commission reject SBC's and CUB's novel tests and, instead, keep to the steady course this Commission has so far charted in order to protect Illinois telecommunication markets against price squeezes. Staff RB at 3-4.

II. How to Define the "Service" Subject to Imputation in this Proceeding

A. Direct Testimony

This is primarily a legal issue, not specifically addressed in Staff testimony.

B. Rebuttal Testimony

This is primarily a legal issue, not specifically addressed in Staff testimony.

C. Legal Argument in Briefs

Staff notes that, in this proceeding, the Commission must decide, among other things, how in what form SBC Illinois' retail business network access lines ("NALs") are subject to imputation as a competitive telecommunications "service" under Section 13-505.1 of the PUA. Staff IB at 10. It is Staff's position that SBC Illinois' NALs are subject to imputation as a stand-alone, individualized service *without regard to any revenues garnered from other competitive services* that SBC Illinois (or a competitive carrier) obtains in conjunction with that service. Staff IB at 10, *citing* Staff Ex. 1.0 (Koch Direct), at 15-19, 22-27; Staff Ex. 2.0 (Koch Rebuttal), at 2, 4-8. In practical terms, Staff

believes the only acceptable description of SBC Illinois' NALs as a competitive "service" for imputation purposes is that of a business customer that (1) has no local or toll usage, (2) has no subscription to any central office features, such as vertical services, and (3) does not generate any switched access revenue for SBC Illinois. Staff IB at 10. Staff notes that its witness, Robert F. Koch, demonstrates in his testimony that *any* inclusion of local or toll usage, central office features or switched access revenues in the imputation test of SBC Illinois' NALs would render the test impotent. Staff IB at 11, citing Staff Ex. 1.0, at 16-17; Staff Ex. 2.0, at 5-8. Staff's position is also shared by Joint CLECs. Joint CLEC Ex. 1.0 (Webber Direct), at 6, 13-20; Joint CLEC Ex. 20.0 (Webber Rebuttal), at 3-18.

Staff notes that SBC Illinois and CUB both urge the Commission to broaden Staff's description to also include local and toll usage, central office features and/or switched access revenues. Staff IB at 11. SBC Illinois and CUB reason that these revenues should be included because CLECs obtain revenues from these other competitive services when offering NALs to business end users. SBC Ex. 1.0, at 9,17-22; SBC Ex. 1.1, at 7-15, 18-27; CUB Ex. 1.0, at 2-14; CUB Ex. 2.0R, at 3-4, 9-13. The SBC/CUB proposal is without merit and is tantamount to reading the imputation test out of the statute. Staff IB at 11.

As Staff demonstrates in its Initial Brief, Section 13-505.1's plain language and legislative history, and past Commission practice demonstrate that SBC Illinois' NALs are subject to imputation on a stand alone basis without regard to revenues from other competitive services used in conjunction with the company's NALs. Staff IB at 12. Staff's treatment of the issue demonstrates that Staff's position (and that of Joint CLECs) represents the proper application of the imputation test to SBC Illinois' NALs. SBC Illinois and CUB's proposal, on the other hand, should be disregarded. Staff IB at 12.

Staff first demonstrates that the plain language of Section 13-505.1 requires that the imputation test be passed on a stand-alone basis. Staff IB at 12 et seq. Section 13-505.1 directs the Commission to define SBC Illinois' NALs for imputation purposes on a stand-alone basis to prevent the company from engaging in price squeeze of competing carriers. Id. Any analysis must begin with the statute itself because it is the best source of legislative intent. Staff IB at 12 (citations omitted).

Staff notes that, in 1992, the General Assembly enacted Public Act 87-0856, which included the imputation requirement as part of the legislature's overall rewrite of Article XIII of the PUA. Staff IB at 12 (citations omitted). Section 13-505.1 states in full:

Sec. 13-505.1. Imputation.

(a) This Section applies only to a telecommunications carrier that provides both competitive and noncompetitive services. If a carrier provides noncompetitive services or noncompetitive service elements to other telecommunications carriers for the

provision by the other carriers of competitive services, switched interexchange services, or interexchange private line services or to other persons with which the telecommunications carrier also competes for the provision by those other persons of information or enhanced telecommunications services, as defined by the Federal Communications Commission, then the telecommunications carrier shall satisfy an imputation test for *each of its own competitive services*, switched interexchange services, or interexchange private line services, that utilize the same or functionally equivalent noncompetitive services or noncompetitive service elements. *The purpose of the imputation test is to determine whether the aggregate revenue for each service exceeds the costs, as defined in this Section, to be imputed for each service based on the telecommunications carrier's own routing arrangements*. The portion of a service consisting of residence untimed calls shall be excluded from the imputation test. The imputed costs of a service for purposes of this test shall be defined as the sum of:

(1) specifically tariffed premium rates for the noncompetitive services or noncompetitive service elements, or their functional equivalent, that are utilized to provide the service;

(2) the long-run service incremental costs of facilities and functionalities that are utilized but not specifically tariffed; and

(3) any other identifiable, long-run service incremental costs associated with the provision of the service.

(b) Notwithstanding the provisions of subsection (a), if a telecommunications carrier permits other telecommunications carriers to purchase interexchange private line services, except those provided under contract or other form of agreement pursuant to the provisions of Section 13-509, under the same tariffed rates, terms, and conditions as any other customer, then such interexchange private line services provided by the telecommunications carrier shall not be subject to the imputation test required in this Section.

220 ILCS 5/13-505.1 (emphasis added).

To paraphrase, Section 13-505.1 applies to incumbent local exchange carriers, like SBC Illinois, that serve more than 35,000 subscriber access lines. Staff IB at 13. Staff argues that, under the statutory provision, "*each*" of SBC Illinois' "competitive services" are subject to imputation where the company provides competing carriers with "noncompetitive services or noncompetitive service elements" that competing carriers need to use as inputs to provide the same competitive service as SBC Illinois. Id., citing 220 ILCS 5/13-505.1(a).

Staff noted that the purpose of the test is to ensure that against a price squeeze in the competitive marketplace. Staff IB at 13. To that end, the imputation test requires that SBC Illinois' revenue (or retail rate) for providing a competitive service equals or exceeds the costs competing carriers *must* face in order to compete against SBC Illinois in the market for that service. Id. Imputation only applies SBC Illinois' competitive services that utilize "noncompetitive services" or "noncompetitive service elements" in provisioning of the same individual competitive service. Id. at 14. For present purposes, and discussed in more detail elsewhere in Staff's Initial Brief, the "noncompetitive services or noncompetitive service elements" are the necessary inputs or bottleneck facilities or equipment that competing carriers must obtain from incumbent carriers, such as SBC Illinois, to provide the same competitive telecommunications service. These bottleneck facilities may include unbundled network elements (or UNEs). Staff IB at 14.

Staff notes that Section 13-505.1 also states that the formula for calculating the costs of service for imputation purposes consists of three components: (1) SBC Illinois' tariffed rates for the noncompetitive services or noncompetitive services elements that are used to provide the resulting competitive service; (2) SBC Illinois' long-run service incremental costs (LRSIC) for facilities and functionalities that are utilized by the competitive service but not specifically tariffed by SBC Illinois; and (3) any other SBC Illinois LRSIC costs associated with the provision of the competitive service. Staff IB at 14.

In short, Staff argues that the plain language of Section 13-505.1 directs the Commission to undertake two analyses. Staff IB at 14. First, SBC Illinois must pass imputation "for *each* of its own competitive services[.]" Id. (emphasis added). Second, the imputation test ensures that SBC Illinois' aggregate revenue (or retail rate) "for each [competitive] service" at issue meets or exceeds the cost of service faced by competing carriers to provide the same competitive service as SBC Illinois. Id. Based on these instructions, Staff argues that the Commission must analyze SBC Illinois' competitive services on an individualized, stand-alone basis without factoring in (or commingling) revenues of *other* competitive services that *may be* associated with the competitive service that is subject to imputation. Id.

Moreover, Staff contends that the plain language of the provision makes no mention of the revenues competitive carriers *might obtain* by offering the same competitive service as SBC Illinois—let alone revenues CLECs obtain from *other* competitive services associated with that service. Staff IB at 15. In Staff's view, the statute simply requires the Commission to compare *SBC Illinois'* retail rate for the competitive service at issue against the company's imputed costs for that service, and determine whether that retail rate is equal to or greater than the imputed costs. Id. Staff observes that there is no mention whatever of the section applying in any way to a non-ILEC, or of the consideration of any non-ILEC revenues. Id. Accordingly, Section 13-

505.1's silence with regard to CLECs dictates that these carriers' *potential* revenues are irrelevant and it would be improper for the Commission to consider them in formulating any imputation test for a specific service. Id., *citing* Illinois Bell Telephone Co. v. Ill. Commerce Comm'n, 203 Ill. App. 3d 424, 438 (2nd Dist. 1990) (stating two germane principles: (1) "the fact that no statute precludes an agency from taking a particular action does not mean that the authority to do so has been given by the legislature"; and (2) "[a]s a matter of statutory construction, the expression of one thing in an enactment excludes any other, even if there are no negative words prohibiting it.").

Staff notes that the same result inures when Section 13-505.1 is read in concert with Section 13-502.5 of the PUA. Staff IB at 15-16. In Section 13-502.5(b), the General Assembly declares that all retail telecommunications services provided to business end users as competitive services, which includes usage and vertical services for those end users. Id.; 220 ILCS 5/13-502.5(b). Further, Section 13-502.5(c) specifically identifies retail vertical services as competitive services. 220 ILCS 5/13-502.5(c). In short, Section 13-502.5(b) and (c) treat usage and vertical services as *separate* competitive services.

In sum, within the context of an imputation test of SBC Illinois' NALs, it is Staff's opinion that the Commission *cannot* include the potential complimentary revenues that may be derived from a business customer's usage or use of vertical services, as SBC Illinois and CUB insist. Staff IB at 16. The plain language of Section 13-505.1 itself and when read in conjunction with Section 13-502.5 make clear that the Commission must define SBC Illinois' NALs, for imputation purposes, as applying to all business customers without regard to their proclivity for complimentary competitive services. As such, the competitive service subject to imputation in this proceeding must be that of a business customer that (1) has no local or toll usage, (2) has no subscription to any central office features, such as vertical services, and (3) does not generate any switched access revenue for SBC Illinois. Id. Any other configuration would, in Staff's view, render the test a pointless nullity. Id.

If Section 13-505.1's plain language were not enough, Staff advances substantial arguments that the legislative history also supports Staff's view that the Commission must define a "service" subject to imputation on a stand-alone basis. Staff IB at 17, et seq. Staff notes that, aside from enacting the imputation requirement, Public Act 87-0856 also amended Section 13-507. Staff IB at 17. Generally speaking, Section 13-507 requires that the aggregate revenue for *all* of SBC Illinois' competitive services must be equal to or greater than the aggregate costs for *all* its competitive services. 220 ILCS 5/13-507. Id. Staff states that the reason for this test is to protect against subsidization of competitive services by noncompetitive services. Id. The logic is that, if it can be shown that the revenue for the company's competitive services as a whole exceeds their costs as a whole, then it cannot be found that these services are being subsidized. Id.

Staff observes that Public Act 87-856 was the product of Conference Committee Report #1 to Senate Bill 511 of the 87th Illinois General Assembly. Staff IB at 17. The House sponsor of the bill was Representative James McPike, while its Senate sponsor was Senator Denny Jacobs. Id. On floor debate, the following statement was read into the record in both the House of Representatives and Senate solely for purposes of legislative intent, as illustrated in the House debates below:

Rep.McCracken: Mr. McPike, I would like to confirm whether I'm correct in certain legislative intent of the Bill. I'd like to read the statement and ask if this is a correct statement of legislative intent. "The legislative intent of the Amendments to Section 13-507 is to establish that common facilities and expenses shall be allocated to noncompetitive services as a group and to competitive services as a group, and shall not be allocated to individual services. *Aggregate revenues for competitive services as a group must be equal to or greater than the aggregate costs, including the combination of imputed tariffed rates on a protective basis for all* ***individual*** *services where required by new Sec. 13-505.1, all other* ***individual*** *services incremental costs, and all common facilities and expenses allocated to competitive services as a group. However, that portion of competitive services which is accounted for by imputation of noncompetitive tariffed rates shall be excluded from the basis for deriving the allocation of common facilities and expenses to competitive services as a group.*" Is that correct, Sir?

Rep. McPike:Yes, Mr. McCracken. That is correct.

Id. at 17-18, citing 87th Ill. Gen. Assem., House Proceedings, May 13, 1992, at 64-65 (colloquy of Representatives James McPike and Thomas McCracken) (emphasis added); 87th Ill. Gen. Assem., Senate Proceedings, May 13, 1992, at 23-24 (colloquy of Senators Denny Jacobs Richard Luft) (same).

The above passage is significant in Staff's view because it describes the process of formulating the aggregate revenue test for Section 13-507, which has subsequently been codified in Code Part 792.200. 83 Ill. Admin. Code § 792.200. Staff IB at 18. Although the particular discussion is in regard to the legislature's amendment to Section 13-507, there are two significant insights that can be garnered from the passage that are germane to the legislature's intent of Section 13-505.1. Id.

First, Staff notes that the aggregate revenue test under Section 13-507 is a single test that is performed on the entire set of incumbent carrier's competitive services at the same time. Staff IB at 19. It is a separate and distinct test from the one conducted for imputation, and its intent is different. Id. In contrast, the aggregate revenue test required for imputation under Section 13-505.1 is limited solely to an incumbent carrier's revenues from one stand-alone competitive service. Id. As such, the "aggregate revenue" test of Section 13-507 and Code Part 792, which implements Section 13-507,

should be applied differently than the test applied under Section 13-505.1 for imputation purposes. Id. Section 13-507's test is an amalgamation of revenues for all of SBC Illinois' competitive services, while Section 13-505.1's test is limited to SBC Illinois' revenues for a single competitive service. Id.

Staff notes that this is significant because SBC Illinois witness Panfil and CUB witness Dunkel have attempted to supplant imputation's "aggregate revenue" test with Section 13-507's aggregate revenue test by introducing revenues from other competitive services into the imputation test of SBC Illinois NALs. Staff IB at 19, citing SBC Ex. 1.0, at 9,17-22; SBC Ex. 1.1, at 7-15, 18-27; CUB Ex. 1.0, at 2-14; CUB Ex. 2.0R, at 3-4, 9-13. Staff notes that Mr. Koch made this distinction clear on cross-examination in response to questions posed by the Administrative Law Judge. Staff IB at 19, citing Tr. 62-69.

Second, Staff notes that Representative McCracken specifically references imputed costs as relating to individual services. As such, the above statement indicates that the sponsors of Public Act 87-0856 intended to subject competitive services to imputation on an "individual service" basis rather than lumping those services together for purposes of imputation. Staff IB at 19, citing Spinelli v. Immanuel Evangelical Lutheran Congregation, Inc., 144 Ill. App. 3d 325, 330 (2nd Dist. 1986) quoting in part 2A A. Sutherland, STATUTORY CONSTRUCTION § 48.15, at 337 (1984) ("statements by the sponsor of the legislation are especially significant [in discerning legislative intent] 'since legislators look to the sponsor* * * to be particularly well informed about its purpose, meaning, and intended effect.'").

Staff next shows that the Commission, in its past imputation decisions, has concluded that, while it has the authority to define the competitive "service" subject to imputation, any Commission-approved "service" definition must serve the statute's fundamental goal—barring incumbent carriers from engaging in anticompetitive pricing behavior that prevents competitive carriers from providing competitive services at competitive rates. Staff IB at 20. In Staff's opinion, those past decisions demonstrate that the Commission has traditionally defined those competitive services subject to imputation on a disaggregated, case-by-case basis because a "narrow" definition of the "service" subject to imputation serves as the best means to accomplish the statute's fundamental goal. Id. In turn, Staff argues, the Commission has repeatedly rejected the use of a broad definition of "service" for imputation purposes because to do so would negate the very purpose of the test. Id. In addition, Staff asserts that the Commission's imputation test has evolved over time to the point where the Commission requires an incumbent carrier's network access lines, such as SBC Illinois' NALs, to pass imputation. Id.

Staff notes that, shortly after Section 13-505.1's enactment, the Commission initiated a rulemaking proceeding to implement the provision. In its initiating order, the

Commission stated that the then-new statute requires incumbent carriers to satisfy an imputation test on a stand-alone basis for *each* of its competitive services. Staff IB at 21. Two years later, in 1994, the Commission determined in its *MCI Complaint Order* that Section 13-505.1 provides the Commission with the authority to define the competitive services subject to imputation. Id. In so doing, the Commission adopted Staff's view that in defining those services the Commission "must examine offerings on a case-by-case basis utilizing all relevant criteria, with its main goal being to prevent and discourage anticompetitive pricing and behavior." Id.

Similarly, in the Commission's *First Alt-Reg Order*, both Staff and Ameritech took the position that the Commission can only determine what services are subject to the imputation "on a case-by-case basis." Staff also argued that "attempting to define what constitutes a [competitive] service *by examining functionalities, or service titles alone* [of SBC Illinois' tariff] may not achieve the fundamental goal of imputation." Staff IB at 21. Staff explained that while these tariff "titles" may "provide meaningful guidance":

[T]he determination of the level of disaggregation for imputation (i.e., what services or elements of services should be subject to imputation) should be mainly driven by the goal of guarding against anti-competitive behavior. In other words, [the Commission must evaluate] whether a competing carrier possibly was being prevented from providing services at competitive rates due to the rates it is charged by [SBC Illinois] for essential, noncompetitive inputs to the competing carrier's service.

Staff IB at 22.

In that order, Staff notes that the Commission again adopted Staff's position when it explained that imputation "tests are intended to determine whether the rates that a[n] [incumbent] carrier charges a competing carrier for certain noncompetitive service elements are discriminatory. [These tests] are used to analyze whether competitors of a carrier, who are also customers of that carrier, are being prevented from providing services at competitive rates." Id.

Staff further notes that in 1995, in the Commission's *Customers First Order*, AT&T and MCI argued, among other things, that Ameritech's unbundled loops and ports that make up its network access lines ("NALs") should be subject to separate imputation tests. Staff IB at 22. Staff disagreed, but claimed that Ameritech's unbundled loops and ports may be subject to imputation depending on Ameritech's rate design. Id.

Ameritech responded that the Commission had no authority to subject its NALs to imputation. Staff IB at 22. Ameritech reasoned that since Section 13-505.1 only explicitly required tests "for switched interexchange services and competitive services" the Commission could not subject its NALs to imputation because NALs were not explicitly listed in the statute. Id. at 23.

The Commission rejected Ameritech's claim, holding that it had the discretion to subject Ameritech's NALs to imputation even though the statute and the Commission's imputation rules did not specifically mention NALs. Staff IB at 23. At the same time, the Commission declined to adopt AT&T and MCI's proposals to subject Ameritech's unbundled loops and ports to separate imputation tests. Id. Instead, the Commission accepted Staff's position that Ameritech's NALs were subject to an imputation-type test whereby the total cost for the unbundled portions of Ameritech's NAL "i.e., the loop, port, [and] monthly connection charges" could not exceed "the total price of the bundled line providing the same services and functionalities." Id.

Staff further notes that, in 1996, in the Commission's *AT&T Wholesale Service Order*, AT&T asked the Commission, among other things, to determine whether Ameritech's wholesale services must pass imputation. Staff IB at 23. Ameritech argued in response that the imputation test only applies to retail service rates, not wholesale service rates. Id. Staff supported AT&T's position and asserted that "Section 13-505.1 requires imputation [of Ameritech's wholesale service rates], and even if it did not, the Commission should require imputation." Id. The Commission concluded that Ameritech's wholesale services were indeed subject to imputation because the intent of the imputation requirement "is to ensure that incumbent LECs (*e.g.,* Ameritech and Centel) are not able to use the prices of their noncompetitive inputs to squeeze their competitors out of the retail markets." Id. From this, the Commission held that the plain language of the PUA does not support Ameritech's claim, nor could the Commission accept such a claim because "incumbent LECs should not be allowed the opportunity to squeeze their competitors out of the retail market[.]" Id. at 23-24

In sum, Staff argues that the above Commission decisions reveal two points. Staff IB at 24. First, the Commission has considerable authority to define the competitive service subject to imputation. Id. Second, the Commission's exercise of its authority to define those services, however, must be performed in a manner fully consistent with Section 13-505.1's fundamental purpose of preventing a price squeeze of competitive carriers. Id.

In its Reply, Staff rebutted several unconvincing arguments made by SBC (CUB also advanced similar arguments) to support its proposition that its business NAL is not a stand-alone service under Section 13-505.1 but, rather, should be considered on an overall basis with other associated competitive services. Staff RB at 4.

Staff first addressed SBC Illinois' claims that neither Section 13-505.1, nor Article XIII's definitions, is helpful in defining what constitutes a "service" for imputation purposes. To the contrary, Staff argues that both provisions are of the utmost use in making such a determination in this proceeding as Staff explained in its Initial Brief.

Staff RB at 4. Staff noted that Section 13-505.1 is completely unambiguous in at least three respects.

First, Staff points out that the statute requires "each" of SBC Illinois' "competitive services" to pass imputation where the company provides competing carriers with "noncompetitive services or noncompetitive service elements" that competing carriers need to use as inputs to provide the same competitive service as SBC Illinois. Staff RB at 4-5 (internal citations omitted). Second, Staff notes that the statute's imputation test ensures that SBC Illinois' retail rate "for each [competitive] service" at issue meets or exceeds the costs of service faced by competing carriers to provide the same service as SBC Illinois. Id., at 5. Last, the statute's silence as to revenues competitive carriers *might obtain* by offering the same competitive service as SBC Illinois or from other associated, but separate, competitive services indicates that it would be improper for the Commission to consider them in formulating any imputation test for a specific competitive service. In sum, then, the plain language of Section 13-505.1 requires the Commission to analyze each of SBC Illinois' competitive services on a stand-alone basis without factoring in (or commingling) revenues from *other* competitive services that may be in some way associated with the competitive service that is subject to imputation. Id.

Staff explained that Section 13-502.5 of the PUA further clarifies Section 13-505.1's mandate, to the extent any clarification is needed, by delineating that SBC Illinois' usage and vertical services are each separate and distinct competitive services when provided to business end users. Staff RB at 5 (internal citations omitted). Id. Further, Code Part 792 of the Commission's rules, which implements Section 13-505.1, make clear that Article XIII's definition of "telecommunications service" is, contrary to SBC's suggestions, neither "unhelpful" nor "circular" for purposes of determining what is subject to imputation. Staff pointed out that Commission rule 792.20 states that a "telecommunications service" as defined in Section 13-203 of the PUA is a "service" subject to imputation if it meets the description set forth in Section 13-505.1. Id. Put differently, Staff explained that an incumbent carrier's *telecommunications service* is subject to imputation when all of the following are met: (1) the service is either a competitive service, switched interexchange service or interexchange service private line services; (2) the incumbent carrier uses its own noncompetitive services or noncompetitive services elements to provide that competitive service; and (3) the incumbent carrier makes those same noncompetitive services or noncompetitive service elements available to competitive carriers so they can provide the same competitive service as the incumbent carrier. Staff RB at 5-6.

Staff concluded that a simple application of Part 792 to the facts of this proceeding reveals that SBC Illinois retail business NAL is subject to imputation on a stand-alone basis. Staff RB at 6. In support of its conclusion, Staff noted that the

company itself admits (in light of the provisions of Section 13-502.5 of the Public Utilities Act, it can scarcely do otherwise) that its retail business NAL is a competitive service, and that service is available to business end users on a stand-alone basis. Further, as Staff pointed out in its Initial Brief, SBC Illinois conceded in both the Commission's *2002 Code Part 792* proceeding and in response to Staff Data Request 1.11 that its loops and ports are two of the three necessary parts that comprise its competitive offering of the retail business NAL. Staff IB at 34. Finally, Staff notes that SBC Illinois concedes--as, again, it must--that it makes its unbundled loops and ports available to competitive carriers as UNEs. In sum, SBC Illinois is mistaken that Section 13-505.1 and Article XIII are "unhelpful", either on their own or as implemented by the Commission's imputation rules. Staff RB at 6.

Staff also points out that SBC Illinois' legislative intent argument is improper, and is contrary to Section 13-505.1's plain language and past Commission decisions. Staff RB at 7. SBC Illinois also postulates -- without citation to any authority -- that the imputation statute "was not drafted with the network access line in mind" but, rather, "was primarily focused on interexchange, switched services like local calling, and private line services" because they "were complete services." SBC Illinois IB at 7. From that proposition, SBC Illinois deduces this since its "network access lines" are not a "complete service" its NALs simply do not fit the model the imputation test was enacted to embrace. *Id.* at 7. The company derives this conclusion despite the fact that it admits that business end users can purchase the NAL on a stand-alone basis, and only receive calls. Staff RB at 7.

Staff points out that SBC Illinois' assertion that the legislature intended to exempt its NALs from imputation on a stand-alone basis is absolutely incorrect, for several reasons. To begin with, SBC Illinois offers *no support* for its novel view of Section 13-505.1's legislative history, other than citing its own witness's unsupported testimony. As the Commission is well aware, expert witness testimony on statutory construction is not only *incompetent* as to statutory interpretation, but also is *improper* and should be stricken *even before an administrative agency*. *Dept. of Corrections v. Ill. Civil Service Comm'n*, 187 Ill. App. 3d 304, 307-08 (1st Dist. 1989) (reversing and remanding an agency decision in part because it both admitted and relied upon expert testimony as to statutory construction). Accordingly, Staff recommends that the Commission disregard SBC Illinois' argument for this reason alone.

Staff notes that even on the merits, however, SBC Illinois' proposition is contrary to the plain language of Section 13-505.1. Section 13-505.1 not only subjects an incumbent carrier's "interexchange service" and "interexchange service private line services" to imputation, but also "*each*" of its "*competitive services*." Staff RB at 8 (internal citations omitted). To accept SBC Illinois' interpretation would require the Commission to read the terms "each" and "competitive service" out of the statute, which, of course, it cannot do. *Primeco Personal Communs. v. Ill. Commerce Comm'n*, 169

Ill.2d 70, 91 (Ill. 2001) (a statute must be construed "so that no term is rendered superfluous or meaningless."). Staff also noted that even if one were to assume *arguendo* that the legislature did not contemplate subjecting the company's retail business NAL to imputation on a stand-alone basis, that fact alone does not render Section 13-505.1 in any way less applicable to these circumstances. Staff noted that the Illinois Supreme Court has long since rejected the proposition, advanced by SBC Illinois here, that the scope of a statutory provision is confined to only those circumstances specifically contemplated by lawmakers. *McDaniel v. Bullard*, 34 Ill. 2d 487, 491 (Ill. 1966). In its *McDaniel* decision, the Illinois Supreme Court held that a statutory provision is fully applicable to situations not initially contemplated by the legislature when (1) the statute is prospective in operation, (2) is phrased in terms comprehensive to cover new situations, and (3) the application of the statute to the new situation would be consistent with the statute's legislative purpose. *Id.* Without question, Section 13-505.1 meets each of the attributes set forth by the *McDaniel* court. Staff RB at 8, n. 6.

Staff also notes that SBC Illinois' attempt to argue that Section 13-505.1 does not apply to its retail business NAL on a stand-alone basis is unavailing due to past Commission decisions. SBC Illinois questions the application of Section 13-505.1 to its NALs merely because it asserts that: (1) its NALs are not a "complete service" subject to imputation (whatever that might be); or (2) its NALs cannot be neatly separated from usage, vertical features, and switched access since a UNE port supports both its NALs and those other named competitive services. The Commission has rejected both of these resurrected arguments in its past decisions. Staff RB at 8.

Staff notes that in 1995, in its *Customers First Order*, the Commission rejected SBC Illinois argument that it had no authority to subject the company's NALs to imputation because that service was not explicitly listed in Section 13-505.1. Staff RB at 9 (internal citations omitted). The Commission held that it had the discretion to subject SBC Illinois' NAL to imputation as a stand-alone service even though the statute and the Commission's imputation rules did not specifically mention NALs. The Commission adopted Staff's position, and concluded that the company's NAL were subject to Staff's "sum-of-the-parts" imputation test *even though* SBC Illinois' NAL were not yet classified as a "competitive service." Id. (internal citations omitted).

A year later, in its *Customers First Compliance Order*, Staff pointed out that the Commission concluded SBC Illinois' UNE port functionality was a "separate element" and severable from the switch and other switch functions, such as usage and vertical services. Staff RB at 9 (internal citations omitted). Ameritech witness Eric Panfil testified that "it was crucial [for the Commission] to recognize that the customer interface on the switch (i.e., the 'port' and all the functionality of the switch) are inseparable" from a network access line. Mr. Panfil further testified that it would be appropriate for the company to price its ports at zero. Staff and intervenors took

positions in opposition to SBC Illinois, and clarified that a "port is the basic non-usage sensitive service which gives the customer access to other switching services."

Staff pointed out that the Commission concluded that Staff's and intervenors' view was "compelling and that zero port pricing [was] contrary to [its *Customers First Order*]." Id. In addition, the Commission concluded that "[a] port is a separate element" from the switch and other switch functions. In sum, SBC Illinois' misguided, and utterly unsupported, argument that the General Assembly intended to exclude its NALs from stand-alone imputation is improper, simply wrong, and contrary to Section 13-505.1's plain language and past Commission decisions. Staff RB at 10 (internal citations omitted).

Staff also noted that SBC Illinois' mischaracterization of Staff's position only succeeds in further undermining the company's theory. In support, Staff points out that SBC Illinois claims it is Staff's position that imputation is required for every competitively tariffed service that can "function on a stand alone basis," and for every "unique rate" offered in SBC Illinois' tariffs. Id. The company then knocks down its newly created straw man by arguing that since the term "stand alone" nowhere appears in connection with the word "service" in the statute, the statute cannot be said to subject "every product which can 'function on a stand alone basis'" to imputation. Id. Further, the company asserts that nothing in the statute requires imputation "for every unique rate" offered in its tariff, nor have such tests ever been performed. Id., at 10-11.

Staff contends that SBC's argument is without merit. To set the record straight, SBC Illinois' characterization of Staff's position is, as noted above, simply incorrect and misleading. Staff RB at 11 (internal citations omitted). It is Staff's view that an incumbent carrier's competitive service is subject to imputation on a stand-alone basis because the statute explicitly states that "*each of [an ILEC's] own competitive services*" is subject to imputation (provided, of course, other criteria are met). 220 ILCS 5/13-505.1(a) (emphasis added). The word "each" is defined in relevant part as "every one of two or more persons or things composing the whole, *separately considered*." *Orr v. Edgar*, 283 Ill. App. 3d 1088, 1096 (1st Dist. 1996) (emphasis added). Thus, when the General Assembly specified "each" of an incumbent carrier's "competitive services" is subject to imputation, it intended for a particular competitive service to be considered separately based on the provision's main goal of preventing a price squeeze. Staff RB at 11.

Staff also noted that a competitive service is only subject to imputation on a stand-alone basis if *all* of the following are met:

- The incumbent carrier uses its own noncompetitive services or noncompetitive service elements to provide that stand alone competitive service;

- The incumbent carrier makes those same noncompetitive service inputs available to competitive carriers so they can provide the same competitive service as the incumbent carrier;

- The incumbent carrier has increased its tariffed rates for those noncompetitive service inputs that competitive carriers must purchase from the incumbent carrier.

In other words, SBC Illinois' characterization of Staff's position is far off the mark. Consequently, it is absurd for SBC Illinois to contend that Staff believes that imputation tests must be performed for every unique rate element contained in the company's tariffs. Staff RB at 11-12 (internal citations omitted).

Staff also contends that SBC Illinois' description of the "price squeeze" barred by Section 13-505.1 is wrong. Staff notes that, aside from attacking Section 13-505.1 and Article XIII as "unhelpful" and "circular," SBC Illinois attempts to re-define what constitutes a "price squeeze" for imputation purposes. The company does this as yet another way to improperly include revenues from other competitive services, such as usage, vertical services, and switched access services, into the narrow imputation test the Commission must perform in this proceeding. The company asserts – again, without citation to any authority - that: "the purpose of a price squeeze test [under the statute] is to promote competitive '*fairness*.'" From this, SBC Illinois fabricates, from whole cloth, the proposition – again, unsupported by any authority -- that the Commission is "require[d], or at least permit[ted],…to evaluate the scope of the 'service' subject to imputation in a policy context so as to promote 'fairness'—for both the incumbent provider and the competitor." Further, the company alleges that is it Staff's view—which it is not—that the purpose of imputation testing is to "protect individual customers or small groups of customers." Staff RB at 12 (internal citations omitted).

Staff concluded that SBC Illinois' proposition is absurd. Staff noted that the imputation statute's purpose is to *prevent and eliminate* a "price squeeze," not construct a "price squeeze" arrangement that, in SBC Illinois' words, "promotes fairness" to "both the incumbent provider and the competitor." The only "fairness" aspect of Section 13-505.1 – "fairness" is a word nowhere to be found in the statute - is its mandate to create a level playing field for competitive carriers because of SBC Illinois' monopoly control of bottleneck facilities at issue in this proceeding. Staff RB at 12 - 13 (internal citations omitted).

Staff noted that SBC Illinois' dubious attempt to undermine and distinguish the Commission's *MCI Complaint Order*, however, warrants examination. SBC Illinois contends that the Commission's order is distinguishable on its facts, and only "stands

for the proposition that separately priced calling plans" are subject to imputation. Also, the company states that the order "does not address the unique situation here where the network access line is [purportedly] not a stand-alone purchasing decision." Staff RB at 13 (internal citations omitted).

Staff explained that while SBC Illinois is correct that the Commission did "not address" whether its NALs are subject to imputation, the Commission, in the *MCI Complaint Order*, stated two guiding principles relevant to this proceeding. *MCI Telecommunications Corp. and LDDS Communications, Inc. v. Illinois Bell Telephone Company: Complaint under Articles IX and XIII of the Illinois Public Utilities Act*, ICC Docket No. 93-0044, 1994 Ill. PUC LEXIS 417 (Order entered Oct. 5, 1994) ("*MCI Complaint Order*"). First, the Commission noted that, as a general rule, the greater the aggregation of service offerings, the greater the chance that an incumbent carrier can engage in a price squeeze and defeat imputation's legislative purpose. *MCI Complaint Order*, at *30. Second, the Commission made clear that, because of the first principle, the Commission must look *beyond* an incumbent carrier's self-description of the service at issue, and examine the offering on a *disaggregated*, case-by-case basis to prevent anticompetitive pricing and behavior. *See* i*d.* at *31-*32 (Commission rejects SBC Illinois' broad definition of the term "service" for imputation purposes, which aggregated different service offerings, because the company simply looked to the offering's "functionality" and "neglect[ed] the potential for anticompetitive pricing and behavior."). It is these principles that SBC Illinois (and CUB) hope the Commission will ignore, which it ought not. Staff RB at 13-14.

Staff also noted that on at least two occasions after its *MCI Complaint Order*, the Commission reiterated and refined these principles in a manner that utterly debunks SBC Illinois and CUB's notion of the statute's price squeeze prohibition. In its *Customer First Order*, the Commission rejected then-Ameritech's reciprocal compensation proposal on imputation grounds, because the proposal would place competitive carriers from the outset in a "loss leader" position if they terminated local traffic on Ameritech's network. The Commission explained that for imputation purposes the issue is "not whether a new LEC ultimately can scrape together revenues from enough sources to be able to afford Illinois Bell's switched access charges." Staff RB at 14, *citing Customers First Order*, at *209-*210.

Instead, Staff pointed out that the Commission determined, the "crucial issue is the effect of a given reciprocal compensation proposal on competition", and whether competition is "viable" for competitive carriers at that level when competing against an incumbent carrier. Id. Put differently, the purpose of imputation is to evaluate whether competitors are placed in a loss leader position at the individual service level when they must use an incumbent carrier's noncompetitive service inputs to provide the same competitive service as the incumbent carrier. The Commission concluded that Ameritech's proposal was "not just or reasonable" because it would force new LECs to

adopt either a premium pricing strategy or use local calling as a "loss leader." Id., at 14-15.

Staff also noted that the Commission rejected Ameritech's "business entry" analysis, which was prepared by its witness, Eric Panfil. Staff RB at 15. That analysis—like Mr. Panfil's analysis in this proceeding—posited that competitors could profitably enter the local exchange market despite paying Ameritech's unreasonably high switched access rates because those carriers can "offer[] a broad array of services" to offset high access rates. Id. (internal citations omitted). The Commission found Mr. Panfil's analysis to be "fundamentally flawed" in part because "[i]ntuitively, it is questionable whether it is prudent to permit an incumbent LEC to demonstrate the reasonableness of its rates with reference to its own conceptualization of the services a competing new entrant would offer." Staff opined that Mr. Panfil's analysis is equally flawed here, and the Commission should give it equally short shrift. Staff RB at 15.

Staff also pointed out that in 1996, in response to the FCC's Notice of Proposed Rulemaking that later resulted in the *First Report and Order*, the Commission reiterated in its comments the above description of the imputation statute's price squeeze prohibition. The Commission made these comments in response to the FCC's request for comments on the scope of state imputation rules. *Id.* The Commission's FCC comments are discussed in more detail below. Staff RB at 15.

Before leaving this issue, Staff notes that its position on the Section 13-505.1 price squeeze prohibition should not come as a surprise to SBC Illinois, because it mirrors the position Staff took in the Commission's *2002 Code Part 792* proceeding. In that proceeding, SBC Illinois stated that the purpose of imputation tests is to "*prevent* price squeezes" not permit them. *2002 Code Par 792 Order*, at *25-*26 (emphasis added). SBC Illinois further explained that a "price squeeze may occur when a carrier provides both a competitive service to end users, and provides a noncompetitive service or service element that is a necessary input to the competitive service to both itself and an equally efficient competitor." *Id.* at *25-*27. SBC Illinois continued with, "a price squeeze occurs if the first firm [the incumbent carrier] chooses to increase rates in the noncompetitive service or service element to the point where it becomes unprofitable for the second firm [a competitive carrier] to provide the competitive service, since the rates for the noncompetitive service or service element are a cost to the second firm." *Id.* The company concluded that "if the rate for the noncompetitive service is greater than [the first firm's] cost, it is possible for the first firm to engage in a price squeeze by dropping the rates on its competitive services without subsidizing the competitive services." *Id.*

Staff noted that SBC Illinois' above description is not the only type of "price squeeze" scenario Staff and Joint CLECs addressed, but it is also the type of price squeeze that the Commission must prevent in this proceeding. Staff RB at 16. SBC Illinois' provides a competitive service to business end users—NALs—that is comprised

of necessary noncompetitive inputs—unbundled loops and ports—that are utilized by SBC Illinois and competitive carriers to provide the same competitive service - indeed, in competition with one another. In the *UNE Loop Order*, the Commission approved SBC Illinois' request to increase its rates for those necessary noncompetitive inputs that competitive carriers depend upon. Since SBC Illinois' TELRIC-based rates for those necessary noncompetitive inputs is now greater than the company's LRSIC for the same inputs, SBC Illinois can engage in a price squeeze by simply maintaining its current retail rates for its competitive NALs. The Commission's task, consequently, is to eliminate that price squeeze. Id.

In short, Staff found SBC Illinois' attempt to redefine Section 13-505.1's price squeeze prohibition is both unsurprising and disingenuous. Staff RB at 17. As the Commission cogently observed in a similar context, "[a]pparently, a prize squeeze is the flip side of arbitrage." And, the Commission likewise observed, "depend[ing] upon whose ox is being gored," the benefiting party—in this case, SBC Illinois—will claim ignorance as to the existence of a price squeeze. SBC Illinois' conduct here fulfills this prophecy by relying upon FCC price squeeze analyses from that agency's Section 271 decisions. As revealed below, the company's appeal to those decisions is also misplaced and simply a thinly-veiled attempt to misdirect the Commission from its mission to eliminate SBC Illinois' ability to price squeeze competitive carriers.

Staff found SBC Illinois' reliance upon FCC "price squeeze" decisions is inapposite. Staff explained that SBC Illinois relies upon three FCC Section 271 decisions to support its erroneous view that the Commission's price squeeze analysis in this proceeding can consider revenues from other competitive services. Staff RB at 17. The company's reliance on those decisions is misplaced for several reasons. First, the Commission's task is not to implement federal law, but to administer its own statute—Section 13-505.1. Staff's previous discussion amply addresses the proper construction of the statute and need not be repeated here. Id. (internal citations omitted).

Second, Staff noted that even if the Commission were charged by the Illinois General Assembly to reconcile the state's imputation statute with federal law price squeeze concepts, and it was not, the FCC decisions themselves reveal how the agency's price squeeze analyses are entirely different from the type required under the PUA and are therefore irrelevant to price squeeze concerns under Section 13-505.1. Staff RB at 18. The FCC performed its price squeeze analyses as part of its *overall* examination of whether to grant RBOCs long-distance authority under the federal act's "public interest" standard. Id. (internal citations omitted). Under that standard, the FCC specifically considers not only competitive carriers' costs, but also their profit margins and revenues from *all* revenue sources, including resale. The FCC considers these additional factors because the agency must make a *general* determination as to whether a relevant local exchange market is open to competition *irrespective* of the mode of entry chosen by competitive carriers. In particular, the FCC's Section 271 price

squeeze analysis sets out to determine "whether competitors are 'doomed to failure.'" Id. (internal citations omitted). If competitive carriers are not "doomed to failure," then the FCC concludes that an RBOC's entry into the long-distance marketplace would be in the *overall* "public interest." Staff RB at 18-19 (internal citations omitted).

In contrast, Section 13-505.1's "price squeeze" analysis is distinct and much narrower and more granular. In SBC Illinois' own words, the imputation statute is "an Illinois-specific response" to the issue of a "price squeeze." Staff RB at 18-19 (internal citations omitted). And, as the company admitted in 1998, the PUA's imputation requirements "are more stringent than an imputation test from [even] an economics perspective[.]" Id. (internal citations omitted). As SBC Illinois further explained in the Commission's *2002 Code Part 792* proceeding, Section 13-505.1's "imputation tests use the rates, where appropriate, charged [by an incumbent carrier] to other carriers, to ensure that a carrier does not anticompetitively increase the price of a noncompetitive service *required and used by a competitor to provide competitive service* to give [the incumbent carrier] a competitive advantage in a downstream product." Id. (internal citations omitted). In addition, SBC Illinois correctly observed that "imputation [under Section 13-505.1] prevents an ILEC from pricing a competitive service so low that an equally efficient provider, who must buy some components from an ILEC, cannot afford to match [the ILEC's] price." Id. (internal citations omitted).

Staff in summary, pointed out that SBC Illinois' own words show that the FCC's "doomed to failure" approach causes it to conduct a much broader price squeeze analysis that considers additional factors that cannot be included under the PUA. Staff RB at 19. The only similarity then between the FCC's "price squeeze" analyses and those required under Section 13-505.1 is that they share the same name. As a result, SBC Illinois' misplaced reliance on the FCC's notion of a "price squeeze" must fail. Staff recommends that the Commission reject SBC Illinois' argument in its entirety. Staff RB at 19-20.

Staff also took issue with SBC Illinois' argument that the Commission cannot engage in "rate-rebalancing" using TELRIC rates, which Staff found fundamentally flawed. Staff noted that SBC Illinois asserts that the Commission would jettison "long-standing" policy if it were to require the company to include UNE loop and ports into the imputed cost of its retail business NAL at TELRIC, rather than LRSIC rates. Staff RB 20 (internal citations omitted). The company also improperly contends that: "the FCC never intended that TELRIC rules dictate state retail rate structures." Id. In SBC Illinois' view, "[i]t would be more than a little perverse for the Commission to adopt an interpretation of state law that would impose federal costing and pricing constraints on its ratemaking authority that the FCC went out of its way to avoid." Id. As Staff explained below, the company's argument is without merit.

To set the record straight, the FCC's *First Report and Order*, to which SBC Illinois cites, make two points clear. First, the FCC elected *not* to establish its own *national* imputation requirement "to detect and prevent price squeezes." Staff RB at 20 (internal citations omitted). Second, the FCC clarified that its decision not to establish such a *national* requirement should not be construed in any manner to hamper the authority of state commissions to implement state law imputation requirements and engage in rate rebalancing. Id. (internal citations omitted).

Staff noted that, in fact, the FCC concurred with state commission commentators, including this Commission, that there is "nothing in the 1996 Act [that] prohibits individual states from adopting imputation rules." Staff RB at 20 (internal citations omitted). Further, the FCC concluded, "[w]hile [a national] imputation rule may be pro-competitive, we will leave the implementation of such rules to individual states." Id. (internal citations omitted).

In short, Staff found the only thing "perverse" to be SBC Illinois' suggestion that the FCC has admonished this Commission against engaging in "rate rebalancing" when the company's UNE rates for noncompetitive inputs for a competitive service exceed its retail rate for that service. Indeed, the Commission's FCC comments show that the Commission would not (and could not) tolerate such a scenario under Section 13-505.1. Staff RB at 21 (internal citations omitted).

In the Commission's words, "competitors will be required to sell [a competitive] service[] as a 'loss leader,' hoping to make up the difference on other services." Staff RB at 21 (internal citations omitted). The Commission then reiterated a portion of its *Customers First Order* where it rejected then-Ameritech's reciprocal compensation proposal on imputation grounds because the proposal would make the competitor a "loss leader" if it terminated local traffic on Ameritech's network. Staff RB at 21-22 (internal citations omitted).

Staff noted that the Commission's own statements reinforces Staff's position that, for purposes of this proceeding, the "crucial issue" is whether it is "viable" for competitors to offer competitive business NALs against SBC Illinois without that service being a "loss leader" from the outset. SBC Illinois clearly would like the Commission to ignore the fact that its increased unbundled loops and ports rates have a "loss leader" effect on competitive carriers. Staff recommends that the Commission recognize SBC Illinois' position for what it is—anticompetitive and neither just nor reasonable. Staff RB at 22 (internal citations omitted).

Staff also noted that aside from misconstruing the FCC's *First Report and Order*, SBC Illinois' assertion that the Commission would jettison its "long-standing" policy if it were to require the company to include UNE loop and ports into the imputed cost of its NALs at TELRIC, rather than LRSIC rates ignores SBC Illinois' long-standing support for this position. Staff RB at 22. Staff pointed out that in the Commission's 1998 *First*

TELRIC proceeding, the Commission established TELRIC rates for SBC Illinois' unbundled network elements, including its unbundled loops and ports, and considered the relationship between TELRIC rates for network elements and Section 13-505.1. Id. (internal citations omitted). SBC Illinois argued that a proper imputation test of its network access lines would consist of, *inter alia*, the company's retail rate for its bundled NAL, "together with the TELRIC costs for a port, price of a loop, and a proportionate share of a service coordination fee[.]" Id. (internal citations omitted).

Staff pointed out, moreover, that SBC Illinois claimed that the Commission could not "direct [it] to lower the prices for its UNEs if a proper imputation test [were] not passed because the lowering of such a price would not permit [SBC Illinois] to cover the prescribed amounts of costs under the [federal] Act, including forward-looking shared and common costs." Staff RB at 23 (internal citations omitted). As a remedy, SBC Illinois argued that "the Commission must permit [the company] to raise the price of [its] corresponding bundled, retail service." Id. Further, SBC Illinois (correctly) stated that allowing the company to raise its bundled retail rate was not only a "question" deferred by the FCC "to the states," but also "the type of 'rate rebalancing' envisioned by the FCC." Id. (internal citations omitted).

Simply put, Staff found that SBC Illinois' position in the Commission's *First TELRIC* proceeding speaks for itself and is, unsurprisingly, the mirror opposite of its position in this proceeding. Strangely enough, the company's former view, as expressed above, is much like that of Staff in this proceeding. Staff recommends that the Commission disregard SBC Illinois' position in this proceeding. Staff RB at 23.

III. Whether UNEs Are "Services" or "Service Elements" for Purposes of the Imputation Requirement

A. Direct Testimony

Mr. Koch states that nothing in Section 13-505.1 or Code Part 792 suggests that UNEs are not services or service elements within the meaning of those provisions. Staff Ex. 1.0 at 8. Indeed, Code Section 792.20 specifically provides that "service" include the term "telecommunications service" as defines in Section 13-203. Id. Mr. Koch further notes that SBC has conceded that the retail NAL is subject to imputation. Id. at 7. Further, Mr. Koch notes that SBC's tariff states that the UNE loop is a "noncompetitive telecommunications service". Id. Finally, Mr. Koch observes that UNE loops are used in the provision of the retail business NAL. Id.

B. Rebuttal Testimony

Mr. Koch does not explicitly address this issue in his rebuttal testimony. *See* Staff Ex. 2.0.

C. Legal Argument in Briefs

As Staff observes elsewhere, the second part of the Commission' inquiry in this proceeding is to determine whether SBC Illinois' unbundled network elements ("UNEs") constitute "noncompetitive services" or "noncompetitive service elements" for purposes of the imputation test. Staff IB at 29. As with Staff's above discussion in Section II, this inquiry is one of statutory construction and those rules of construction are applicable to our discussion below. Id. This inquiry ultimately reveals that SBC Illinois' UNEs, *at minimum*, are "noncompetitive service elements" for purposes of imputation under Section 13-505.1. Id. Further, UNEs constitute "noncompetitive services" because SBC Illinois' tariff designates its unbundled loops as a noncompetitive telecommunications service, and that designation is dispositive for purposes of this proceeding. Id. These conclusions are fully supported by both Section 13-505.1 itself when construed in concert with other sections of Article XIII of the PUA, and by past Commission decisions. Id.

Staff notes that Section 13-505.1 provides that a particular competitive service offered by SBC Illinois is subject to imputation if that competitive service utilizes the same or functionally equivalent "noncompetitive services" or "noncompetitive service elements" the company makes available to competitive carriers so those carriers can provide the same competitive service. Staff IB at 30. Neither Section 13-505.1 nor Article XIII of the Public Utilities Act, however, provides specific definitions for the terms "noncompetitive service" and "noncompetitive service elements" as used in the imputation provision. Id.

Illinois courts have long held that when a statute does not define a term, the court will assume that the word has its ordinary and popularly understood meaning. Staff IB at 30 (citations omitted). In doing so, a court must consider the legislative intent and the context in which the term is used. Id. In reading the text of a statute, the statutory provision should not be read in isolation, but in the context of the Act as a whole. Id. And, as a corollary, later statutory amendments to a statute should be read together with the original statutory provisions left unchanged by the legislature. Id. Moreover, in determining the intent of the legislature, the court may properly consider not only the language of the statute, but also the reason and necessity for the law, the evils sought to be remedied, and the purpose to be achieved. Id. Based on these rules, we first turn to Public Act 87-0856 to discern the meaning for the terms "noncompetitive service" and "noncompetitive service element" because that enactment produced the imputation requirement. Id.

Aside from adding Section 13-505.1 to Article XIII of the PUA, the Staff notes that Public Act 87-0856 also added and amended other sections of that Article. Staff IB at 31 (citations omitted). A review of those sections reveals that the General Assembly interchangeably used the terms "noncompetitive telecommunications service" and "noncompetitive service." Id. For example, newly-enacted Sections 13-505.1 through 13-506.1 all use the term "noncompetitive service" in either in their text, or their title, or both. Id. In particular, Sections 13-505.6 and 13-506.1 each use the term "noncompetitive service" in its title, but the term "noncompetitive telecommunications services" in its text. Section 13-506.1 uses both terms in its text. Id.

Staff argues that these facts indicate that when the General Assembly used the term "noncompetitive services" in Section 13-505.1, it intended for that term to mean "noncompetitive telecommunications services," as defined in Section 13-210. Staff IB at 31. As a result, it is Staff's position that SBC Illinois' competitive services are subject to imputation if that competitive service utilizes the same or functionally equivalent "noncompetitive telecommunications services" the company makes available to competitive carriers so they can provide the same competitive service. Id.

Staff argues that a "noncompetitive telecommunications service" is a telecommunications service that is not reasonably available from more than one provider. Staff IB at 32 (citations omitted). Staff notes that Section 13-502 provides SBC Illinois (or any other carrier) with the initial discretion to designate a given telecommunications service as either competitive or noncompetitive via tariff. Id. If SBC Illinois' tariff classification for a particular service has gone into effect without challenge (by either the Commission or another party), Staff asserts that the tariff classification is presumed correct and has the force and effect of law. Id. (citations omitted).

Staff notes that SBC Illinois' tariff has classified its UNE loops as a noncompetitive telecommunications service. Staff IB at 33 (citations omitted) Accordingly, SBC Illinois' tariff classification is dispositive for purposes of this proceeding, which, in turn, means the company's UNE Loops are deemed "noncompetitive services" for imputation purposes.

Staff observes that SBC Illinois and CUB urge the Commission to ignore this fact by pointing to FCC's decisions that hold that UNEs are not telecommunications services, but network elements. Staff IB at 33. What these parties fail to realize, according to Staff, is that the FCC's determination is completely inapposite for two reasons: First, the FCC made its determinations in the context of *federal law*, *not state law*; and second, FCC decisions are not binding on the Commission nor are they even relevant given the unique context of state law. Id., (citations omitted).

Even *assuming arguendo* that SBC Illinois' tariff classification were not dispositive to this proceeding—*and Staff is clear that it is*—the structure and text of

Section 13-505.1 and Article XIII of the PUA indicate that SBC Illinois' UNE Loops are "noncompetitive service elements" for purposes of imputation. Staff IB at 33. To be sure, Public Act 87-0856 offers little guidance as to the meaning of the term. Id. After all, the term only appears in Sections 13-505.1 and 13-505.4 and only in the disjunctive after the term "noncompetitive service." Id. (citations omitted). Staff notes that, since neither Article XIII nor the PUA itself defines the term "elements," the Commission must resort to its ordinary and popularly understood meaning. Id.

Staff observes that the term "elements" is ordinarily defined as "a constituent part; a distinct part of a composite device." Staff IB at 33. Given the context within which the term appears, Staff concludes that the General Assembly's use of the word "elements" obviously refers to the constituent or distinct noncompetitive part or noncompetitive parts that comprise a competitive telecommunications service. Id. at 33-34. Based upon these insights, the rhetorical question then becomes whether SBC Illinois' UNE Loops and Ports are, ordinarily speaking, constituent or distinct parts of a competitive telecommunications service. Id. at 34.The answer, in Staff's view, is that they very clearly are. Id. No party contests the veracity of this statement, not even SBC Illinois. Id.

Staff notes that in the Commission's *2002 Code Part 792 Order*, SBC Illinois conceded that its loops and ports are two of the three parts that comprise its offering of competitive business network access line service. Staff IB at 34. As SBC Illinois stated, "For example, *business network access lines have been subject to imputation for several years*. Individuals familiar with telecommunications and, therefore, Staff personnel understand that *network access lines are basically provisioned through a loop, port, and a cross connect*." Id. (citations omitted). Further, Staff notes that in response to Staff Data Request 1.11, SBC Illinois stated, "A retail network access line includes both a loop and switch port, therefore each is a necessary element of the network access line." Id.

Moreover, Staff argues that one need look no further than Section 13-216 of the PUA to draw the same conclusion that SBC Illinois' unbundled loops and ports are "noncompetitive service elements" for imputation purposes. Staff IB at 34. Likewise, Staff notes that Section 13-216 defines the term "network element" as, in pertinent part, "a facility or equipment used in the provision of a telecommunications service." Id. Thus, Staff argues, SBC Illinois' unbundled loops and ports unquestionably qualify as "network elements." Id.

In addition to the text and structure of Section 13-505.1 and Article XIII of the PUA, Staff notes that the Commission has also characterized an ILEC's unbundled loops as "noncompetitive services" or "noncompetitive service elements" for imputation purposes. Staff IB at 35. Staff points out that, in its *GTE North Order*, the Commission had to determine, among other things, whether GTE North's (now Verizon) CentraNet

service, a PBX-type service, was subject to imputation. GTE North argued that since no competitors were offering a similar service in the company's service territory, the company's CentraNet service was not subject to imputation. Id. (citations omitted). There Staff agreed with GTE North's position. Id. AT&T and MCI, on the other hand, argued that the company's CentraNet service was subject to imputation irrespective of whether competing carriers directly competed with GTE North's service. Id. These parties reasoned that imputation was required because the competing carriers were using the company's noncompetitive facilities to provide other types of competitive services. Id. Specifically, AT&T and MCI stated that they were using GTE North's "*local loops and access switching facilities*" to provide their competitive services. Id. (emphasis added)

Staff notes that the Commission agreed with AT&T and MCI and concluded that GTE North's CentraNet service was subject to imputation based on the plain language of Section 13-505.1. Staff IB at 36 (citations omitted). Staff observes that, aside from recounting GTE North's status as a carrier offering both competitive and noncompetitive services, the Commission held that the company's provisioning of local loops and access switching facilities to AT&T and MCI amounted to the offering of "non-competitive services or service elements" for imputation purposes. Id. Moreover, Staff observes, the Commission ordered GTE North to use its tariff price for local loops and access switching services in its imputation test for the company's CentraNet service. Id.

In its Reply Brief, Staff emphasized that the Commission's determination as to whether SBC Illinois' UNEs are "noncompetitive services" or "noncompetitive service elements" for imputation purposes is a matter of statutory construction and Commission judgment. Staff RB at 23. Staff's Initial Brief set forth and applied those relevant rules of statutory construction and past Commission decisions, and drew two conclusions: (1) SBC Illinois' UNEs are "noncompetitive services" because the company's tariff classification is dispositive for imputation purposes; and (2) SBC Illinois' UNEs are, at minimum, "noncompetitive service elements." Id.

Staff noted that the Joint CLECs reached the same result as Staff, but through different means. Staff RB at 24 (citations omitted). SBC Illinois and CUB, in contrast, rely exclusively upon the "telecommunications services"/"network elements" distinction for their claim that UNEs are neither "noncompetitive services" nor "noncompetitive service elements" for imputation purposes. Staff RB at 25 (citations omitted). SBC Illinois and CUB both find support in the FCC's *federal law* determination that UNEs are not "telecommunications services," but "network elements." Id. While CUB relies exclusively upon the FCC's determination, SBC Illinois goes one step further and argues that this distinction also arises under the PUA based on the Article XIII's definitions for those terms, the Illinois Appellate Court's *Globalcom* decision, and the Commission's recent *Project Pronto* Order. From these sources, SBC Illinois concludes

that UNEs are not "noncompetitive services" under Section 13-505.1. Id. (citations omitted).

Similarly, Staff noted, the company asserts that "[i]f UNEs are not '[noncompetitive] services,' [then] they cannot be 'service elements' either." *Id.* SBC Illinois, however, fails to back up its assertion with anything other than circular reasoning as discussed below. Staff RB at 25 (citations omitted). Finally, the company claims that Staff's tariffing argument is "irrelevant" because the company does not provide UNEs pursuant to tariff, but rather through interconnection agreements, and SBC Illinois will "at some point in time" withdraw its tariffs. Id.

In reply, the Staff refutes SBC Illinois and CUB's argument that UNEs are not "noncompetitive services" under Section 13-505.1. Staff demonstrates once again that SBC Illinois' tariff classification of its UNEs as "noncompetitive telecommunications services" is dispositive and qualifies them as "services" for purposes of this proceeding. Further, Staff shows that when SBC Illinois provides UNEs to CLECs via interconnection agreement, those UNEs are deemed "telecommunications services" under Section 13-206, and, in turn, may qualify as "services" for imputation purposes. Finally, Staff debunks SBC Illinois' argument that UNEs are not "noncompetitive service elements" based on both the text and structure of Section 13-505.1 and the Article XIII and simple common sense.

Staff noted that in its Initial Brief Staff demonstrated that UNEs qualify as "services" for imputation purposes based on the text, purpose, and structure of Section 13-505.1 and Article XIII of the PUA. Staff RB at 26 (citations omitted). Staff explained that when the General Assembly used the term "noncompetitive services" in Section 13-505.1, it intended for that term to mean "noncompetitive telecommunications services," as defined in Section 13-210. Id. Staff further explained that SBC Illinois' competitive services were subject to imputation if that competitive service utilizes the same or functionally equivalent "noncompetitive telecommunications services" the company makes available to competitive carriers so they can provide the same competitive service. Id. Staff concluded that since SBC Illinois' tariffs classified its UNE loops as a noncompetitive telecommunications service, that tariff classification was dispositive for purposes of this proceeding based on case law interpreting Section 13-502 and the Commission's *GTE North* imputation decision. Id.

To counter Staff's argument, Staff noted that SBC Illinois and CUB enlist resources beyond the company's tariff in support of their claim that UNEs are not "noncompetitive services" for purposes of imputation. Staff RB at 26-27. First among these is the FCC's conclusion that UNEs are "network elements," not "telecommunication services." Di. (citations omitted). Staff reiterated that the company and CUB's reliance on the FCC's *federal law* determinations are inapposite because, in this proceeding, the Commission is implementing *state law*, *not federal law*. Staff RB at

27. And, given the unique context of this state law proceeding, those FCC decisions are neither binding nor relevant. Id.

Staff noted that, in a similar vein, SBC Illinois argues that the same distinction exists under the PUA as evidenced by Article XIII's definitions for the terms "telecommunications services" and "network elements." Staff RB at 27 (citations omitted). In addition, the company points to the Illinois Appellate Court's *Globalcom* decision and the Commission's recent *Project Pronto Order*, which have both recognized that distinction. Id. (citations omitted). Staff noted that from these sources, SBC Illinois deduce that UNEs are not "noncompetitive services" because of the "telecommunications services"/"network elements" distinction. Id. As revealed below, SBC Illinois' reliance on the Article XIII's definitions and the above decisions is misplaced because the Commission cannot look beyond the unambiguous terms of SBC Illinois' tariff, which states that the company's unbundled loops are "non-competitive telecommunications services." Id. (citations omitted).

Staff's discussion below of the *Globalcom* decision illustrates Staff's argument. In *Globalcom*, the issue before the court was whether SBC Illinois properly charged Globalcom early termination fees when the CLEC converted special access circuits to EELs. SBC Illinois made the EELs available on an unbundled basis pursuant to Section 13-801(d)(3) under an "interim compliance tariff," which set forth the requisite rates, terms, and conditions to obtain EELs and other UNEs. Staff RB at 27-28 (citations omitted).

SBC Illinois argued that the Globalcom triggered the fees because its conversion from special access circuit to EELs constituted a "termination of service" under the ILEC's "interim compliance tariff." Staff RB at 28 (citations omitted). Globalcom and the Commission, however, claimed that the conversion did not amount to a termination. Since SBC Illinois' tariff *did not* define "termination of service," the court looked to FCC's *First Report and Order* and Article XIII's definitions to resolve the ambiguity. Id. (citations omitted). Based on the FCC's decision and Section 13-216, the court held that Globalcom's conversion to EELs was a "termination of service" under the tariff. Id. Accordingly, the court concluded that it was permissible for SBC Illinois to charge the CLEC early termination fees. Id. (citations omitted).

Globalcom's facts demonstrate that it offers no guidance to the Commission in this proceeding because the court dealt with an ambiguous tariff term, which required the court to look *beyond* the tariff to other sources to resolve the matter. As the Illinois Supreme Court recently explained, "[a]lthough a utility tariff is not a legislative enactment, *its interpretation is governed by the rules of statutory construction*." *Adams v. Northern Ill. Gas Co.*, 211 Ill. 2d 32, 64 (Ill. 2004) (emphasis added). Staff has already shown SBC Illinois' tariff is *unambiguous* in that it explicitly classifies the company's unbundled loops as "*non-competitive telecommunications services*." Staff

RB at 28 (citations omitted). As a result, SBC Illinois' reliance on the "telecommunications services"/"network elements" distinction is inapposite because the Commission in this proceeding is clearly confronted with an *unambiguous* tariff provision, and Illinois case law requires the Commission to interpret that tariff as plainly written. Id. (citations omitted).

Similarly, Staff noted that SBC Illinois' citation to the Commission's *Project Pronto Order* does nothing to advance its cause because that proceeding was a reopened tariff proceeding, while this proceeding is opened pursuant to SBC Illinois' *Petition*. Staff RB at 29, *compare* Project Pronto Order, at 2-3 (detailing the docket's procedural history as a tariff proceeding initiated by SBC Illinois) *with* SBC Illinois Petition, at 1 (stating that its Petition was filed "in compliance with the Commission Order in Docket No. 02-0864," which is now a closed tariff proceeding). Simply put, the Commission's *Project Pronto Order* is limited to its circumstances because in that proceeding, by reopening the docket, the Commission had the statutory authority to enter an order to modify SBC Illinois' tariffs. In contrast, in this proceeding, the Commission is confined to the scope of SBC Illinois' *Petition*. A review of SBC Illinois' Petition shows that at no point has the company requested a Commission investigation of its current tariff classification of its unbundled loops. Accordingly, the Commission has no such authority to modify or ignore the terms of SBC Illinois' tariffs. Moreover, it is Staff's position that SBC Illinois' attempts to undermine or down-play the effectiveness of its UNE loop tariff is tantamount to a collateral attack on the Commission's order in Docket No. 02-0864, which did not disturb that or any other tariff classification. Staff RB at 29 (citations omitted).

Finally, Staff notes that SBC Illinois contends that Staff's tariffing argument is "irrelevant" because the company provides CLECs with unbundled loops pursuant to interconnection agreement, not tariff. Staff RB at 29-30 (citations omitted). SBC Illinois further asserts that its tariffs are merely temporary in light of the 7th Circuit Court of Appeal's *Bie* decision and that they will soon be withdrawn. Id. *citing* Wisconsin Bell v. Bie, 340 F.3d 441, 442-45 (7th Cir. 2003).

Staff found that SBC Illinois' argument falls flat and asks too much of the Commission for several reasons. Staff RB at 30 (citations omitted). First, the *Bie* decision in no way absolves SBC Illinois of its state law obligation to file or honor its tariffs. The company's notion that it may withdraw its tariff is simply one of misdirection and a gross misreading of the case. At best, *Bie* stands for the proposition that state commissions cannot force incumbent carriers to file tariffs so that competitive carriers can purchase services *in lieu of* negotiating interconnection agreements with the incumbent carriers. Id. (citations omitted). Put differently, the concern identified by the Seventh Circuit, *and the basis for preempting the state tariff provision at issue*, was the that the state tariff provision permitted a CLEC to obtain services from a tariff without going through the Section 252 negotiation process. In short, SBC Illinois' state law

tariffing rights and duties, as Staff described in its Initial Brief, are fully effective as subsequent state and federal decisions make clear. Id. (citations omitted). As a result, SBC Illinois' tariff designation is dispositive for purposes of this proceeding. Staff RB at 30-31 (citations omitted).

Second, Staff notes that as a practical matter, SBC Illinois has executed literally hundreds of interconnection agreements with CLECs, and many of these agreements either reference SBC Illinois' tariffed rates for UNEs or expressly permit CLECs to order out of SBC Illinois tariffs for UNEs and other products and services. Staff RB at 31 (citations omitted). As a result, SBC Illinois' claim that it only provides UNEs to CLECs pursuant to interconnection agreement is exaggerated. Id.

Third, Staff notes that as a legal matter, Staff believes there is some strength to Joint CLECs' argument that when SBC Illinois provides UNEs to CLECs via interconnection agreement, those UNEs qualify as "telecommunications services" under Section 13-203. Staff RB at 31 (citations omitted). As Joint CLECs correctly note, Section 13-203 defines a "telecommunications service," in pertinent part, to include "interconnection arrangements." Id. (citations omitted).

In addition, Staff shares Joint CLECs' view that it is reasonable to deduce from Section 13-505.1(a)'s text and legislative purpose that the provision "encompasses UNEs provided by SBC to CLECs" because both CLECs and SBC Illinois rely upon those UNEs to provide the same competitive retail service. Staff RB at 31 (citations omitted).

In Staff's view, however, the above legal theory requires further development because Joint CLECs do not explain how it squares with Section 13-216's definition of "network element." Section 13-216 defines a "network element" as "a facility or equipment used in the provision of a telecommunications service." At first blush, the terms "network element" and "telecommunications service" may be, but not necessarily mutually exclusive. Staff RB at 32 (citations omitted).

Before moving on to discuss whether UNEs are "noncompetitive service elements," Staff makes the following observations as to CUB's Initial Brief. CUB generally concurs with SBC Illinois' argument that UNEs are not "services" for imputation purposes because of the so-called "telecommunications services"/"network element" distinction. Staff RB at 32 (citations omitted). CUB, however, performed no statutory construction analysis whatsoever and simply repeated the unsupported testimony of its witness, Mr. William Dunkel. As Staff has explained previously, expert testimony as to statutory interpretation is both *incompetent* and *improper* even in the administrative context. *See supra*, § II, A, 1. *citing Dept. of Corrections v. Ill. Civil Service Comm'n*, 187 Ill. App. 3d 304, 307-08 (1st Dist. 1989). As a result, Staff only

discussed CUB's position above to the extent that it mirrors SBC Illinois'. Staff RB at 32.

Staff further noted that CUB makes an incorrect claim that the Commission's June *UNE Loop Order* has already predetermined that UNEs are not "services" subject to imputation. Staff RB at 32 (citations omitted). Even a cursory review of the *UNE Loop Order,* however, reveals that the Commission was merely summarizing SBC Illinois' position, rather than making a legal conclusion. In short, CUB is clearly mistaken that the Commission's *UNE Loops Order* has predetermined the outcome in this proceeding. Staff RB at 32 (citations omitted).

Staff also found that CUB's discussion of the UNE *Loop Order* also demonstrates its fundamental lack of understanding of how imputation operates. The *UNE Loop Order* makes clear that "the plain language of [Section 13-505.1] [requires] imputation tests [for] *competitive services*, not the noncompetitive services that are at issue in this proceeding [i.e., the proper TELRIC rates for SBC Illinois' *unbundled loops*]." Staff RB at 33 (citations omitted). In other words, imputation tests are required for SBC Illinois' *competitive services*, such as its retail business NALs, which is supposed to be the focus of Section II of each party's brief. The fact that UNEs are "noncompetitive services"—as even the *UNE Loop Order* describes them—has no bearing on whether UNEs constitute "noncompetitive services" or "noncompetitive service elements" for purposes of establishing SBC's imputed costs for its retail NALs under Section 13-505.1(a)(1)-(3). If anything, the Commission's statement in its *UNE Loop Order* that SBC Illinois' unbundled loops are "noncompetitive services" proves Staff's point that UNEs *are* "noncompetitive services" for imputation purposes. Staff will neither dwell nor rely on that statement because the Commission specifically declined to predetermine the matter—a point that CUB fails to grasp. With that said, Staff moves on and demonstrates below that UNEs are, at minimum, "noncompetitive service elements" for imputation purposes. Id.

Staff noted that in addition to being "noncompetitive services," Staff's Initial Brief also explained that SBC Illinois' UNEs are "noncompetitive service elements" for purposes of Section 13-505.1. Staff RB at 34 (citations omitted). Staff determined that while the term "noncompetitive service" was interchangeable with the term "noncompetitive telecommunications service," the term "noncompetitive service elements" was ambiguous because the word "elements" was neither defined in Article XIII nor the PUA. Id.

Consistent with accepted rules of statutory construction, Staff then endeavored to define the word based on its ordinary meaning and in accord with Section 13-505.1 legislative purpose. Staff RB at 34 (citations omitted). Staff deduced that the word "elements," as it is used in the term "noncompetitive service elements," refers to the constituent or distinct noncompetitive part or parts that comprise a competitive

telecommunications service. Id. Further, Staff logically concluded (largely through common sense) that SBC Illinois' UNE Loops and Ports are "noncompetitive service elements" for imputation purposes because the record undeniably reveals that loop and ports are two inputs necessary to offer competitive business network access line service. Id.

Staff noted that SBC Illinois, however, posits that "[i]f UNEs are not 'services,' [then] they cannot be 'service elements' either." Staff RB at 34 (citations omitted). Yet, the company provides little more than a riddle wrapped inside an enigma to explain its position. Id. As best as Staff can decipher it, SBC Illinois' argument derives from four confusing premises:

- Since UNEs did not exist in 1992, they cannot be considered "service elements";

- "'[S]ervice element[s]' [are] equivalent to rate element[s] within a 'service' that [are] separately priced, since rate elements *did* exist in 1992;

- SBC Illinois alone has the power to identify and "to selectively impute only certain rate elements in situations where not all rate elements within a 'service' are used by competitors"; and

- The legislature's 2001 enactment of the term "network elements" "clarifies" that "UNE are not 'service elements' within the meaning of Section 13-505.1."

Staff RB at 34-35 (citations omitted).

In short, SBC Illinois' position seems to be that UNEs are not "service elements" for imputation purposes because only it has the ability to identify service elements. In addition, the company appears to contend that it alone decides what "elements" CLECs need to provide a "service." Staff RB at 35 (citations omitted). From this, it seems clear that what SBC Illinois really saying is that CLECs no longer need unbundled loops and ports to compete against SBC Illinois because CLECs have resale and intermodal entry options. Id.

Staff found that SBC Illinois' argument, however, snaps under its own convoluted logic for several reasons. SBC Illinois' first premise that "UNEs cannot be 'service elements' because UNEs did not exist in 1992" is easily refuted. A review of the Commission's February 1992 *Third Interim Teleport Order* shows that the Commission was very interested in establishing state interconnection policy for local exchange competition. Staff RB at 35-36 (citations omitted). In fact, the Commission's order, *which proceeded the enactment of Section 13-505.1 by three months*, called upon Staff to investigate through workshops "the additional interconnections which are necessary

and/or appropriate for the development of broad and effective local exchange services competition, such *as unbundling of local loops from other network services*[.]" Id. (citations omitted). Moreover, the Commission directed Staff to issue a report on July 1, 1992, summarizing the comments of all interested parties. *Id.* In sum, contrary to SBC Illinois' assertion, the concept of unbundling did exist in 1992 even though it may have not been available to competitive carriers.

Staff also pointed out that the Illinois Supreme Court has long-rejected SBC Illinois' legal theory that the scope of a statutory provision is shackled to only those circumstances present at the time when the statute became law. Staff RB at 36, *citing McDaniel v. Bullard*, 34 Ill. 2d 487, 491 (Ill. 1966). Put differently, the fact that unbundled loops and ports were not coined as "network elements" or "unbundled network elements" in 1992 has no bearing on whether they qualify as "service elements" under Section 13-505.1 today. The *McDaniel* Court properly instructs that the Commission must examine whether Section 13-505.1 is (1) prospective in operation, (2) phrased in terms comprehensive enough to cover UNEs, and (3) its application to UNEs would be consistent with the statute's legislative purpose. Id. (citations omitted).

Staff found that without question, Section 13-505.1 meets each of the *McDaniel* Court factors. As Staff also noted in its Initial Brief, since the word "element" as used in the term "noncompetitive service element" is not defined in the statute, that word must be given not only its ordinary and popularly understood meaning, but also must be construed with reference to the purposes and objectives of the statute. Staff RB at 36-37, *citing M.S. Kind Associates, Inc. v. Mark Evan Products, Inc.*, 222 Ill. App. 3d 448, 450 (1st Dist. 1991). Staff previously identified that the word "element" is ordinarily defined as "a constituent part; a distinct part of a composite device." Id. at 37 (citations omitted). And, in the context within which the word appears, the General Assembly used the word "element" to refer to the constituent or distinct noncompetitive part or parts that comprise a competitive telecommunications service. Id. Moreover, in concert with Section 13-505.1's legislative objective to prevent a price squeeze of competitive carriers, it is obvious that SBC Illinois' UNE Loops and Ports are "noncompetitive service elements" for imputation purposes because the record undeniably reveals that loop and ports are two inputs necessary to offer competitive business network access line service. Id. (citations omitted).

Staff also concluded that SBC Illinois' second and third premises—"service elements" are really "rate elements" and only the company can identify and "selectively impute" them—are entirely without merit. Staff RB at 37. It is simply inappropriate for SBC Illinois to suggest that "service elements" are really "rate elements" when the company provides *absolutely no support for its proposition*. In addition, SBC Illinois does not even tell the Commission in any *objective sense* what constitutes a so-called "rate element." Moreover, SBC Illinois' description that it alone has the power to identify and "to selectively impute only certain rate elements in situations where not all rate

elements within a 'service' are used by competitors" is unsettling. Id. (citations omitted). Put differently, what SBC Illinois seems to be saying is that the General Assembly delegated to incumbent carriers the arbitrary power to say what the law is and determine when something is a "service element" that must be imputed by the incumbent carrier. Illinois courts have made clear that it is unconstitutional for the General Assembly to delegate lawmaking authority to a private person or group. Staff RB at 37-38, *citing People v. Pollution Control Bd.*, 83 Ill. App. 3d 802, 807-08 (4th Dist. 1980). As a result, the Commission should reject SBC Illinois' interpretation because it would render the statute unconstitutional. Id., at 38, *citing Northwest Airlines, Inc. v. Dept. of Revenue*, 295 Ill. App. 3d 889, 893 (1st Dist. 1998) ("an interpretation which renders a statute unconstitutional or otherwise invalid should be discarded.").

Likewise, Staff found SBC Illinois' final claim that UNEs are not "service elements" because the General Assembly amended the statute by adding the definition of the term "network element" in 2001 is simply not credible. Staff RB at 38. As one court explained in a similar context, "[i]t is anomalous to suggest that a section of the law can derive its meaning from a definition which *was not in existence on its effective date*." Id., *citing University Hospital v. State Employment Relations Bd.*, 63 Ohio St. 3d 339, 587 N.E.2d 835 (Ohio 1992) (emphasis added). Traditional rules of statutory construction provide that later statutory amendments to a statute should be read together with the original statutory provisions left unchanged by the legislature. These rules of construction demonstrate that, if anything, the Section 13-216 definition for the term "network element" must be read in harmony with the term "service elements." Id. (citations omitted).

In turn, Staff argues that SBC Illinois' reliance on the Illinois Supreme Court's decision in *People v. Shepard* is inapposite. Staff RB at 38 (citations omitted). In that case, the supreme court had to resolve a conflict between three Public Acts of the 86th General Assembly (86-266, 86-442, and 86-604) and one Public Act from the 87th General Assembly (87-754). Id., *citing* 152 Ill. 2d 489, 494-98 (Ill. 1992). All four Public Acts amended two interrelated-statutes, Sections 401 and 407 of the Illinois Controlled Substances Act. Id. These sections were interrelated and addressed the same subject because Section 407 explicitly referenced Section 401. Id.

The issue was whether the changes made by the first two Public Acts (86-266 and 86-442) were carried forward into Public Act 87-754 even though Public Act 86-604 left them out. Staff RB at 39 (citations omitted). The court explained that as general rule when multiple public acts of the *same* General Assembly conflict, the most recent of those enactments controls. Id. The supreme court held that the general rule did not apply because Public Act 87-754 sufficiently manifested the General Assembly's intent to carry the changes made by Public Acts 86-266 and 86-442 forward despite being left out of Public Act 86-604. Id. (citations omitted). The supreme court concluded that the General Assembly's enactment of Public Act 86-604 without including the language

contained in Public Acts 86-266 and 86-442 was merely a "legislative oversight" and the defendant was properly charged with a crime. Id., at 38-39 (citations omitted).

In short, Staff explained that the *Shepard* Court dealt with successive legislative enactments to the *same* explicitly interrelated statutory provisions, which rendered them internally inconsistent. Staff RB at 39. In contrast, there is no conflict between Section 13-505.1 and Section 13-216 of the PUA because (1) the provisions are not explicitly interrelated, (2) the General Assembly did not amend Section 13-505.1 when it added the term "network element" to Article XIII of the PUA, (3) the term is not even used in the imputation statute, and (4) the term "network element" only appears in sections unrelated to the imputation statute. Thus, no conflict exists between Sections 13-216 and 13-505.1. As a result, Section 13-216 is complementary and can (and should) be read in harmony with the term "noncompetitive service element" as it appears in Section 13-505.1. Staff RB at 39-40, *citing McTigue v. Personnel Bd.*, 299 Ill. App. 3d 570, 589 (1st Dist. 1998) (If two interpretations of a statute are possible, then the one that gives all words in the statute some meaning will be the one that is most reasonable.)

IV. Issues Related to Specific Tests

Mr. Koch testifies that the purpose of imputation is to foster competition in the telecommunications market in Illinois, by protecting against anti-competitive pricing in the form of a "price squeeze." Staff Ex. 1.0 at 9. Mr. Koch states that a price squeeze occurs when a supplier of an essential facility reduces the margin between the price it charges for that facility and the price that it charges for a competitive retail product using that facility. Id. at 9-10. This can result from either an increase in the price of the essential facility, or a decrease in the price of the competitive product. Id. at 10. The imputation test requires a minimal margin to exist between the essential facility and competitive product. Id.

Mr. Koch states that imputation prevents price squeezes in the following manner: when a competitor cannot provide a competitive service without the use of a noncompetitive service (or service element), the incumbent local exchange carrier that provides the noncompetitive service has a potential advantage over other carriers. Staff Ex. 1.0 at 10. Although the market for the *retail* service in question is classified as competitive, the incumbent carrier controls the market for *noncompetitive elements* necessary to provision the competitive service. Id. The imputed cost, in essence, is a proxy for the cost that the competitive carriers incur in order to provide the same service at retail. Id. If the incumbent carrier prices the competitive services below its imputed cost, it is assumed that competitive carriers will not be able to operate in the market. If the incumbent carrier is permitted to engage in this type of pricing, the market for the competitive service will become decreasingly competitive over time. Id. In order to prevent such practices and insure a level playing field for provision of the competitive

service, Section 13-505.1 places restrictions on the amount that the incumbent local exchange carrier can charge for the competitive service in the form of a price floor on the incumbent's retail provision of the service. Id. That price floor is equal to the imputed cost (to the competitor) of providing the service. Id. at 10-11.

Mr. Koch testifies that, under Code Section 792.30(c), imputation tests are required where two conditions are met. Staff Ex. 1.0 a 6. First, the service – in the case the retail business NAL – must be one subject to imputation, which is to say a competitive offering of a carrier that provides both competitive and non-competitive services. Id. at 6-7. There is no question that the retail business NAL is such a service. Id. Second, there must be a rate change for a noncompetitive service or service element that is utilized in the provision of the competitive service. In Mr. Koch's opinion, this is satisfied as well; the Commission recently authorized SBC to raise its UNE loop rates, and UNE loops are unquestionably utilized in the provision of the retail business NAL. Id.

Mr. Koch states that the imputation test establishes a statutorily required price floor that ensures that the cost incurred by a competitor to provide a service is at or below the rate charged by the incumbent carrier for the same retail service. Staff Ex. 1.0 at 11. Mr. Koch further testifies that the imputation test compares the retail revenue realized by the incumbent carrier for a particular service, to the imputed cost that reflects the costs that its competitors would face in offering the identical service. Id. To satisfy the test and thereby protect against a price squeeze, the imputed cost must be less than or equal to the retail revenue. Id. As a formula, this test could be expressed in its simplest form as:

Imputed Cost □ Retail Revenue

Id.

Mr. Koch observes that, once the exact service subject to imputation is defined, determining the retail revenue for the test is fairly straightforward. Staff Ex. 1.0 at 12. It usually is as simple as identifying the appropriate rate for the service from a tariff page. Id. For certain services, however, Mr. Koch states that it may be necessary to make assumptions regarding other factors that affect the rate level, such as minutes of use or mileage distances. Id. Mr. Koch observes that, mathematically, retail revenue for the test can usually be expressed as follows:

Retail Revenue = Tariff Rate for Service Subject to Imputation

Id.

Mr. Koch testifies that the imputed cost is defined in Section 13-505.1 and Code Part 792.40(a)(3) as the sum of the tariffed rates for the noncompetitive services

or services elements utilized to provide the service; plus the long run service incremental costs ("LRSICs") of facilities and functions that are utilized but not specifically tariffed; plus any other identifiable LRSICs associated with the provision of the service. Staff ex. 1.0 at 12. Mr. Koch further observes that, in practice, the task of developing imputed costs is a two-step process. Id. First, it is necessary to identify all of the various LRSIC values for the various imputed cost components. Id. Second, the LRSIC for all noncompetitive services or service elements must be replaced by their tariffed rates. Id. Mr. Koch expresses this mathematically as follows:

Imputed Cost = LRSICs for all components of service – LRSICs for components that are considered noncompetitive services + tariffed rates for those components that are considered noncompetitive services

Id. at 12-13

The formula for the imputation test then becomes:

LRSICs for all components of service – LRSICs for components that are considered noncompetitive services + tariffed rates for those components that are considered noncompetitive = Tariff Rate for Service Subject to Imputation

services
Id. at 13.

Mr. Koch testifies that the foundation for these imputation tests is the relationship between the UNE Loop rate and the retail network access line charge. Staff Ex. 1.0 at 13. When the other relevant cost and revenue elements are included, the imputation test in its most basic form is expressed as:

Imputed Cost = UNE Loop Rate + UNE Port Rate + Cross Connect Rate + SCF Retail Revenue = NAL+ EUCL

Id.

Mr. Koch advocates inclusion of end-user common line charge (EUCL) revenues in the test because the EUCL has been established to recover a portion of the cost for access lines, namely the interstate non-traffic sensitive costs of the NAL. Staff Ex. 1.0 at 14. Mr. Koch observes that SBCI charges a EUCL to all retail access line customers for which an imputation test is performed. Id. Mr. Koch further observes that the same interstate costs that are recovered by the EUCL on the retail side are also included in the TELRIC costs of the UNE loop and port developed by SBCI. Id. As such, Mr. Koch considers it only proper to include SBCI's EUCL rate on the revenue side of the equation. Id. Mr. Koch states that the tests provided by SBCI in this proceeding include the EUCL on the revenue side as well. Id.

Mr. Koch states that an imputation test must be performed on all competitive retail services that are subject to imputation and are affected by the increase in UNE loop rates. Staff Ex. 1.0 at 14. Mr. Koch points out that Section 13-502.5(b) provides that all retail telecommunications services provided to business end users by a telecommunications carrier subject to alternative regulation (such as SBCI) are competitive. Id. at 14-15. Mr. Koch observes that, in this instance, the services impacted are retail business access lines, ISDN lines, COPTS coin lines, COPTS basic lines, and STF lines and must therefore pass imputation. Id. at 15. Furthermore, Mr. Koch states that any and all competitive service packages that include, or "bundle" one or more of the types of lines described above with other telecommunications services must also pass imputation. Id. Staff, states Mr. Koch, believes that if the test is passed under the most basic of conditions (i.e. for a business customer that has no local or toll usage, does not subscribe to any central office features, and generates no switched access revenue for the company) then it follows that SBCI's more complex service offerings would likely meet the imputation criteria as well. Id.

Staff, states Mr. Koch, strongly believes that the statute requires an imputation test for every competitively tariffed service that can function on a stand-alone basis, and for every unique rate offered for that service in the tariff. Staff Ex. 1.0 at 15-

16 Specifically, Staff looks to the following portion of Section 13-505.1 as providing guidance on this issue:

> *"…the telecommunications* ***carrier shall satisfy an imputation test for each of its own competitive services****, switched interexchange services, or interexchange private line services, that utilize the same or functionally equivalent noncompetitive services or noncompetitive service elements."*
>
> *220 ILCS 5/13-505.1(a). emphasis added*

Mr. Koch observes that Code Part 792 also provides some guidance in that it consistently uses the phrase "for each service" when describing when an imputation test must be filed. Staff Ex. 1.0 at 16. Further, states Mr. Koch, SBCI's tariffs include separate and distinct definitions for services such as business NALs, local usage, and the various central office features. Id. Mr. Koch states that if one were to argue that these separately rated functionalities can only be considered as part of one service, it would follow that SBCI's entire competitive tariff has incorrectly defined these functionalities in error. Id.

Mr. Koch states that, if the basic imputation test is passed, this will protect against price squeezes. Staff Ex. 1.0 at 16. Mr. Koch testifies that, to include revenue for services other than the retail network access line in the test for the retail network access line would necessarily weaken the ability of the test to protect against price squeezes in the marketplace. Id. Mr. Koch observes that, as additional revenue for services other than the network access line are added to the imputation test, the effectiveness of the test becomes increasingly compromised precisely because these revenues from additional services *do not make up* or *are not part* of the network access line. Id. at 16-17. Furthermore, notes Mr. Koch, the revenue for services such as local usage and central office features normally have a significant level of margin (i.e., the revenue realized from them greatly exceeds the cost of production). Id. at 17. Mr. Koch opines that the danger of including additional levels of usage and features in the test for the business NAL is that, as the level of usage assumed in the test increases, the percentage of customers that achieve the level of usage in the test decreases. Id. Consequently, the percentage of customers receiving any protection against price squeezes decreases at the same time. Id.

Mr. Koch states that no usage or features should be used in the imputation test in this proceeding, since none are included in the SBC base retail business NAL rate. Staff Ex. 1.0 at 17.

Mr. Koch testifies that business customers can and do purchase the NAL. Staff EX. 1.0 at 18. For the basic access line services, Mr. Koch considers it quite likely

that some customers purchase the service for the sole purpose of having dial tone and have no intention of making outgoing telephone calls. Id. Mr. Koch gives as an example of this type of customer a small business such as a restaurant that offers take-out or delivery service. Id. Mr. Koch notes that use of a phone to make outgoing calls may cause a potential customer to not be able to reach the business to make a purchase, and therefore the manager of such an operation would have an incentive to prohibit such use of the phone. Id. Mr. Koch notes that another business may have the phone strictly as a means to have reliable access to emergency services. Id. Therefore, states Mr. Koch, to include any level of retail usage revenue in the test would render the test ineffective to protect the marketplace for such customers. Id.

Regardless of this, notes Mr. Koch, telephone customers have a wide range of demand for usage and features. Id. Thus, states Mr. Koch, to assume any level of demand for usage and features as being "appropriate" for the test necessarily weakens the test so that it cannot insure against price squeezes in markets for customers with lower call volumes than that assumed in the test. Id. Conversely, the only way to ensure that the market for all types of customers is protected against a price squeeze is to require that the test be passed under the most basic conditions. Id.

Mr. Koch observes that all of the LRSIC costs included on the imputed cost side have been replaced by rates for noncompetitive services. Staff Ex. 1.0 at 19. It is Staff's interpretation of Section 13-505.1 that whenever a noncompetitive rate exists for an imputed cost item, it must be included in the test. Id. Naturally, the UNE loop rate corresponds directly to the type of retail business network access line rate for which the test is being performed. Id. Mr. Koch notes that the UNE port rate, cross connect rate, and service connection fee are all essential items in retail access line provisioning, as well, and each has its own corresponding noncompetitive tariff rate. Id.

A. Issues Common to the Parties' Proposed Imputation Tests

Mr. Koch describes SBCI's tests as follows:

- Scenario (1), which includes revenue for network access lines, usage, and features;

- Scenario (2), which includes only revenue for the stand-alone network access line service; and

- Scenario (3), which has identical revenue to the first scenario but develops its imputed costs via the UNE-Platform.

Staff Ex. 1.0 at 20-21

Mr. Koch generally endorses the tests performed by Joint CLEC witness James Webber, as being generally consistent with the ones that Mr. Koch himself submitted. Staff Ex. 2.0 at 2-3.

Mr. Koch observes that the results of the first two scenarios are included in Schedule ELP-D1 to SBC Illinois Exhibit 1.0, while the results of the third scenario are included in Schedule ELP-D2. Staff Ex. 1.0 at 21. Mr. Koch notes that the imputation tests were filed as work papers supporting the testimony of SBCI witness Eric Panfil. Id. Mr. Koch further notes that the twelve tests in each scenario are basically a set of tests for four separate retail services in each of the three access areas in SBCI's service territory: business NAL, ISDN direct, COPTS coin line, and COPTS basic line. Id.

Mr. Koch attached to his testimony the statutorily required imputation tests for this proceeding. Staff Ex. 1.0, Schedule 1.03. Based on these tests, Mr. Koch observes that Business NALs in Access Area B and C, as well as all of the COPTS Coin and COPTS Basic fail the imputation test required by Illinois law. Staff Ex. 1.0 at 27.

1. Inclusion of Nonrecurring Charges ("NRCs")

a. Direct Testimony

Mr. Koch states that Staff is strongly of the opinion that Section 13-505.1 requires an imputation test – on a stand-alone basis – be performed and passed for every competitively tariffed service that can function on a stand-alone basis. Staff Ex. 1.0 at 15-16. Inclusion of revenues from additional sources is improper. Id. at 16.

b. Rebuttal Testimony

Mr. Koch states that it is improper to use average revenues from multiple services in conducting an imputation analysis for the retail business NAL. Staff Ex. 2.0 at 5-7.

c. Legal Argument in Briefs

Staff witness Mr. Koch does not include NRCs in his imputation tests. In the process of constructing his tests, Mr. Koch found it unnecessary and improper to include such items. Mr. Koch excluded NRCs from his tests because the rate for the business network access line service is not designed to recover the upfront cost of establishing the line connection. Staff Ex. 1.0 at 16. Costs associated with establishing service are recovered separately in SBC's line connection and service order charges. The rates for NRCs are designed to recover the entire cost associated with establishing service, and are paid on an upfront basis when a customer

commences service. There is, accordingly, no need for NRC charges to be included in the retail business NAL imputation test. The Staff, moreover, has consistently excluded NRCs or, for that matter, any separately rated functionality from its imputation tests for NALs in prior proceedings. See generally, the Direct Testimony of Patrick Phipps in Docket 98-0860 (Staff Ex. 5.0); the Direct Testimony of Robert Koch in Docket 02-0864 (Staff Ex. 4.0). Staff IB at 36.

Staff noted that Joint CLEC witness Mr. Webber does not take a position as to whether it is appropriate to include NRCs and their corresponding costs in the imputation test. Rather, he indicates that SBC often waives or discounts NRCs in an attempt to entice customers, and that this fact is not reflected in SBC's imputation analysis in this proceeding. Joint CLEC Ex. 1.0 at 43. Mr. Webber concludes that SBC's use of NRC revenue in its tests skews any meaningful analysis and should be removed. *Id*. However, he does not go so far as to indicate that the costs associated with initially establishing service should also be removed. Staff IB at 37.

In contrast, Staff points out that SBC witness Mr. Panfil disagrees with Mr. Webber's assertion that NRCs should be discounted to reflect the Company's retail promotions. SBCI Ex. 1.1 at 22, 23. Mr. Panfil claims that when SBC offers such promotions, it must file imputation tests showing that the retail service passes a separate imputation test reflecting that promotion. Staff agrees with Mr. Panfil in that, when the Company offers such a promotion, it must make a showing that imputation concerns are satisfied. As noted above, however, the Staff does not believe that NRCs should be a part of the stand-alone imputation test primarily because NRCs are designed to recover their own costs. However, in instances were these NRCs are waived as a promotional offering, it is necessary that these costs be recovered via the recurring NAL rates. Under these limited circumstances, Staff believes that an imputation test that includes NRC revenue and costs would be necessary. Staff IB at 37.

In its Reply Brief, Staff agreed with SBC that it could choose to change its rate structure so that recurring charges are designed to recover these up-front costs and, if SBC re-designed its rate structure, it would be wholly appropriate to include these costs in the imputation test for retail business NALs. Staff RB at 41. As SBC indicates, whenever it files a promotional tariff that waives NRCs, a separate imputation test is filed that reflects this waiver. Id. Staff concurs with this approach in such an instance. However, the fact remains that, under SBC's current rate structure, retail business NAL rates are not designed to recover nonrecurring costs. As long as this remains the case, it would be improper for the retail business NAL imputation test to include nonrecurring cost and revenues. Id.

2. Use of LRSIC or TELRIC Costs for the Port

a. Direct Testimony

Mr. Koch testifies that SBC's scenario 2 is based on "narrow" revenue assumptions, and is therefore acceptable to that extent. Staff Ex. 1.0 at 25. However, Mr. Koch notes that the imputed cost per NAL is developed using the long run service incremental cost ("LRSIC") of the port, rather than tariffed noncompetitive UNE rate. Id. It is Mr. Koch's opinion that this is improper. Id.

Mr. Koch testifies that the UNE port rate rather than the port LRSIC should be used for the following reasons: the port is a noncompetitive element of the retail business access line. Staff Ex. 1.0 at 26. Accordingly, because there is a tariff rate for the UNE port, it is Staff's reading of Section 13-505.1 and Code Part 792.40(c) that the tariff rate must be imputed in the test. Id. Further, Staff notes that CLECs are not charged the LRSIC when they order the port functionality; rather, they are charged the UNE port rate. Id. Imputation is intended to prevent a price squeeze, and this is only accomplished by choosing the costs that are most reflective of those faced by the CLECs. Id. Because the LRSIC of the port is lower than the UNE port rate, the imputed cost presented in this scenario by SBCI is underestimated. Id.

b. Rebuttal Testimony

Mr. Koch does not address this matter in his rebuttal testimony. See Staff Ex. 2.0.

c. Legal Argument in Briefs

Staff contends that the port is a necessary element of the retail business access line. This element has a specific noncompetitive tariff rate in the UNE port. Therefore, as Mr. Koch explained, Section 13-505.1 of the PUA and Code Part 792.40(c) require that the tariff rate must be imputed in the test. Staff Exhibit 1.0 at 12, 19, 26. Mr. Koch further testified that CLECs are not charged the LRSIC when they order the port functionality; rather, they are charged the UNE port rate. Id., at 26. Imputation is intended to prevent a price squeeze, and this is only accomplished by choosing the costs that are most reflective of those faced by the CLECs. Because the LRSIC of the port is lower than the UNE port rate, the imputed cost presented in this scenario by SBC is underestimated. Id. Joint CLEC witness Webber agrees with Mr. Koch's assessment. Joint CLEC Ex. 1.0 at 39; Staff IB at 38.

Staff noted that in direct testimony, Mr. Panfil argues that UNEs are not services or service elements. SBCI Ex. 1.0 at 4. Mr. Panfil does not go so far as to specifically reject the need for any imputation tests resulting from the UNE loop increases ordered in Docket 02-0864. Id. Rather, he merely indicates that the need for a test is primarily a

legal issue to be addressed in SBC's legal brief. Id. It was not until Staff specifically challenged SBC to make a policy statement regarding this issue (Staff Ex. 1.0 at 9), that Mr. Panfil admitted in rebuttal testimony that SBC does not believe that imputation tests have been triggered as a result of Docket 02-0864. Staff IB at 38.

Staff also pointed out that SBC conveniently uses its determination that UNEs are not services or service elements to argue that the UNE port should not be imputed on the cost side of our tests. SBCI Ex. 1.1 at 6. Further, Mr. Panfil points to the fact that some CLECs actually provision their own switch to conclude that UNE ports should not be part of the imputation test. SBCI Ex. 1.1 at 26, 27. Also, Mr. Panfil challenges Mr. Koch's and Mr. Webber's assertions that the UNE port must be in the imputation test because it has been designated as noncompetitive in SBC's tariff. Id. Staff is not persuaded by Mr. Panfil's argument. Mr. Panfil is simply not considering the specific requirements of the statute and code part. Staff IB at 38-39.

In its Reply Brief, Staff noted that Section 13-505.1 of the PUA requires that the UNE port must be included in the imputation test. Staff RB at 41. In Staff view, this is a straight-forward determination, as the port is a necessary element of the retain business NAL and it has a tariffed noncompetitive rate. If UNEs are to be considered services or service elements, this conclusion is academic. SBC, however, takes a different view. SBC makes two unpersuasive arguments as to why it believes that the port LRSIC is the more important component of imputed cost. Id.

First, SBC contends that "[c]ost elements should be imputed only when competing providers have no choice (or almost no choice) but to obtain them from SBC Illinois." Staff RB at 41 (citations omitted). SBC then states that because CLECs "purchased over 25% of unbundled loops on a stand-alone basis" providing "the switching themselves." Id. Based upon this presumption, SBC then concludes that the remaining roughly 75% of CLECs "*choose* to obtain a UNE port as part of their service provisioning process []does not determine whether the rate must be imputed." Id., at 41-42. Staff agrees with SBC in that the cost element to be imputed should be a bottleneck facility. Id., at 42. As a noncompetitive service, the UNE port is just that. The fact that only 25% of competitors provide their own switching is an indication that it is not economically feasible for the majority of competitors to self-provision. Section 13-209 of the PUA requires that a service must be reasonably available from more than one provider before it can be considered a competitive service. Id. A conclusion that no feasible alternative provider exists, at least for a reasonable number of CLECs, for the UNE port is strongly supported by the fact that the UNE port remains classified as a noncompetitive element. Moreover, both Section 13-801 and TA 96 are still the law of the land and SBC is still required to provide these so called "cost elements" under its existing unbundling obligations. Id.

Staff also notes that SBC contends, in opposition to Staff's position, that "the mere fact that the UNE switch port is designated as 'non-competitive' in the tariff is not determinative of the need to include the port in the imputation test." SBC IB at 21-22. As much as SBC might like to think that this is the case, a plain reading of the statute requires the imputation of these rates. Staff RB at 42, *citing GTE North Inc.: Proposed filing to restructure and consolidate the local exchange, toll, and access tariffs with the tariffs of the former Contel of Illinois, Inc.*, ICC Docket Nos. 93-0301/94-0041 (consol.), 1994 Ill. PUC LEXIS 436, at * 161 (Final Order, October 11, 1994) (the Commission ordered GTE North to use its tariff price for local loops and acess switching services in its imputation test for the company's CentrNet service). The only exception might be where certain essential facilities are not offered via tariff, but solely through interconnection agreements. In such a case, Staff would argue that the base rate offered to all carriers in such an agreement would be the appropriate rate to impute. Such is not the case for the UNE port, however. Id.

Staff notes that SBC argues that that there is a "logical 'disconnect' between Staff's and the Joint CLECs' insistence that, on the one hand, usage and feature costs and revenues *may not* be included in the imputation analysis and that, on the other hand, the UNE port rate *must* be used." Staff RB at 43 (citations omitted). Staff does not dispute that usage and features are made available with the purchase of a UNE port. However, the question at hand in this proceeding is how to impute the cost of provisioning a business NAL, and the answer is that the imputed cost must include a UNE port because it is an essential element for many carriers. Id. Further, even though the functionality to provide usage and features is available on the UNE port, there is no guarantee that customers will purchase these services. The logic advanced by SBC presupposes that all such services will be provided to end-users. Id.

B. Issues Specific to SBC Illinois' Proposed "Broad" Imputation Test

Mr. Koch observes that SBC scenario 1 – the "broad" test, including revenues from usage and vertical features – is improper. Staff Ex. 1.0 generally, and at 22 et seq. Mr. Koch notes that, in addition to the revenue for the retail NAL and the End User Common Line Charge (EUCL) provided in the Staff tests, this SBC scenario also includes revenues for average local usage, toll, and central office features on the retail side of the business NAL and ISDN direct imputation tests. Id. at 22. SBC Scenario 1 does not provide a test for any one specific service that is offered in the company's retail tariffs. Id. Rather, it combines revenues from several separately tariffed services. Id.

In Mr. Koch's opinion, the revenue assumptions included in SBCI's Scenario 1 would render the test completely ineffective. Staff Ex. 1.0 at 23. Mr. Koch testifies that these imputation tests would no longer be useful to protect CLECs from

price squeezes for business NALs – in other words, the tests would no longer serve the purpose for which imputation was established. Id. Since the test includes revenues from several individually tariffed services, Mr. Koch asserts that it does not constitute a useful or valid imputation test for any one of those services. Id. In Mr. Koch's opinion, this is clearly illustrated in the table contained in his direct testimony at page 23, which lists the margin by which the rates in each access area pass SBCI's test along side the corresponding retail rates for business network access lines. Id. Mr. Koch notes that, because the margin exceeds the access line rates in each access area, each of these access line rates could be reduced to *zero* and still pass SBCI's imputation test. Id. Mr. Koch points out that, as currently configured, the SBC test advanced in scenario 1 would only protect very high-volume customers from the effect of a price squeeze. Id

Mr. Koch notes that SBC scenario 3 is essentially the same as the first scenario, except that the UNE port is included in the imputed cost side of the test as opposed to the UNE LRSIC. Staff EX. 1.0 at 26. Mr. Koch observes that the revenue side of the tests in this scenario is identical to the revenue side in the Scenario 1 tests and for the same reasons leads to an ineffective test due to the inappropriate inclusion of revenue for usage and features. Id. Mr. Koch further observes that the imputed cost side of the test is improved because it includes the UNE port rate. Id. However, Mr. Koch points out that, just as the revenue side of test inappropriately includes the usage and features revenue, the imputed cost side of the test in this scenario includes the same inappropriate assumptions regarding the average level of usage and features. Id. Therefore, in Mr. Koch's opinion, the tests provided under this scenario are also deficient. Id.

1. Accuracy of Data Used to Develop Usage, Feature and Switched Access Revenues

a. Direct Testimony

b. Rebuttal Testimony

c. Legal Argument in Briefs

Staff notes that both it and the Joint CLECs are of the opinion that usage, feature, and switched access revenue do not belong in the imputation test. Staff Ex. 1.0, at 15-16; Joint CLEC Ex. 1.0, at 10-13. Nonetheless, Joint CLEC witness Webber took issue with the accuracy of the data SBC provided to develop its usage, feature, and switched access revenue figures used in its imputation tests. Id., at 41-45. Chief amongst Mr. Webber's complaints were that the data provided did not come from billed activity, and a concern that 80% of usage revenue presented in SBC's tests did not include discounts. Staff IB at 39.

Staff did not take issue with the source of the data provided by SBC. The data source in question is the annual aggregate revenue test filing, which SBC routinely uses as a source for demand figures. Staff finds this to be an acceptable source. Staff also did not address Mr. Webber's concern that 80% of SBC's usage revenue, as used in its imputed cost analysis, did not contain discounts. Regardless, Staff is of the opinion that, if SBC failed to include an accurate portrayal of usage discounts in imputation tests, the tests would necessarily be skewed. As Staff argues elsewhere in this brief, it does not believe that the revenue for usage and features should be included in the test as a threshold matter. *See, generally,* Section II of this brief, as well as Subsection (B)(2) below. If the Commission were to decide that this revenue should be in the test, however, then it would only be appropriate to reflect the revenue the Company actually receives after discounts have been factored. Staff IB 39-40.

SBC witness Mr. Panfil argues that the exclusion of certain discounts is not a significant issue, as the percentage of its total customer base that receives discounts is low due to the fact that term commitments are necessary to obtain such discounts. In as much as these discounts are not included in SBC's imputed cost calculation, the revenue for these figures will be inflated. Staff is therefore of the opinion that such discounts for usage, where they may exist, would need to be factored into the imputed cost if SBC's proposed tests were accepted. Staff IB at 40.

In its Reply Brief, Staff found pointed out that This is an issue primarily contested by SBC and the Joint CLECs. Staff RB at 43. As Staff noted, revenue for usage and features, as a threshold matter, should not be included in the test. Id. If, however, the Commission decides that this revenue should be in the test, Staff finds the demand data used in SBC's imputation tests, which comes from their annual aggregate revenue test filing, to be an acceptable data source. Id.

The Joint CLECs identified concerns with SBC's calculation of revenues for usage, features, NRCs, and switched access. Joint CLEC IB at 20. Staff did not address any specific concerns identified by Joint CLEC witness Webber regarding these calculations. Rather, Staff merely indicates that, if the Commission were to decide that revenue for these items to be a part of the test, then the revenue for these items should reflect any and all discounts offered by SBC. Staff RB at 43.

2. Use of Averages to Develop Usage, Feature and Switched Access Revenues

a. Direct Testimony

Mr. Koch notes that, even if the margins by which SBCI's proposed test passed imputation were relatively small, the use of average revenue and costs for usage and

central office features would not be proper. Staff Ex. 1.0 at 24. Mr. Koch states that Section 13-505.1 requires that each service must pass, and it can only do so on a stand-alone basis, and that any level of usage and feature revenue would necessarily weaken the ability of the test to provide against a price squeeze. Id.

Staff notes that over half of SBC's business NAL customers generate less than average usage revenue and generate less than average revenue for central office features. Staff Ex. 1.0 at 24. Mr. Koch considers it important to note that, by including these additional service revenues on the revenue side of the test, it follows that the imputed cost side of the test will necessarily also inappropriately have values for these services. Id. Mr. Koch testifies that, just as using average revenue for usage and features is inappropriate, so is including average costs for these services; such averages simply do not belong in the test. Id.

Mr. Koch observes that SBCI claims that, because CLECs typically target high volume customers, the figures used in the SBCI tests are probably underestimated, a claim which Mr. Koch notes is so far unsubstantiated. Staff Ex. 1.0 at 25. Further, Mr. Koch points out that Section 13-505.1 and Code Part 792 do not address whether a typical CLEC currently operating in the market is doing so at a profit; rather, the statute and the Code Part require that the test be passed for the specific retail services in *all* cases, and not just under the most favorable of conditions for the ILEC. Id.

b. Rebuttal Testimony

Mr. Koch considers Citizens Utility Board witness William Dunkel's position that average revenue from multiple services should be used in the imputation test to be improper. Staff Ex. 2.0 at 7.

c. Legal Argument in Briefs

Staff points out that the imputation tests proposed by SBC in this proceeding include average revenues for local usage, central office features, and switched access in addition to the retail NAL and EUCL. SBCI Ex. 1.0 at 7. By combining revenues from several separately tariffed services, such tests do not comply with the requirements of Section 13-505.1. Staff Ex. 1.0, at 16. As was discussed above in Section II of this brief, tests must be performed on a service-by-service basis as a statutory condition. The generous inclusion of such revenue diminishes the ability of the test to fulfill its statutory intent – to prevent against price squeeze. Staff IB at 40-41.

In direct testimony, Staff witness Mr. Koch testified that the assumptions in SBC's proposed imputation tests render the tests useless. Staff Ex. 1.0, at 16-17, 24. Mr. Koch provided a table in direct testimony (*Id*., at 23), which lists the margin by which SBC witness Panfil's proposed tests for retail business NAL pass imputation (*i.e*. the

revenue surplus) alongside the retail rates for SBC's retail NALs. This table clearly indicates that SBC's retail business NALs would pass the imputation test proposed by Mr. Panfil even if the rates for this service were reduced to zero in each access area.

Staff found Mr. Koch's table to be a dramatic indictment of SBC's approach to constructing imputation tests. Reducing retail rates to zero is an extreme example, as rates could not possibly be reduced further. Naturally, such an action would be prohibited by the Commission's cost of service rules. Yet Mr. Koch's hypothetical example clearly shows that SBC's imputation test would not protect against a price squeeze even under such an implausible scenario. Staff IB at 41.

SBC, by using the averages that it does in its tests, in effect is saying that a prize squeeze analysis is not relevant unless it becomes unprofitable to offer service to its highest margin customers. In response to Staff Data Request RFK 1.05, SBC indicates that a majority of its business NAL customers have less than average usage revenue and that majority of its business NAL customers have less than average revenue for central office features. This demonstrates that SBC's test sets the bar mathematically at a level were only the market for the top 34% to 40% of its customers would ever be protected from a price squeeze. Such protection would only occur if imputed costs were to rise dramatically from their current level, as the table above shows that there is a very comfortable margin of revenue over imputed cost presently. Staff IB at 42.

Nonetheless, Staff stresses that the tests proposed by SBC would not be appropriate even if the margins were not as large as shown in the table above. The retail NAL must pass imputation on a stand-alone basis, and the inclusion of any extraneous revenues from other services would necessarily weaken the ability of the test to protect against a price squeeze for the retail NAL. Staff IB at 42.

Staff noted that Joint CLEC witness Webber agrees with Staff regarding the use of average revenue for usage, features, and switched access in the imputation test. Specifically, Mr. Webber identifies as being particularly relevant Staff's conclusions that Section13-505.1 of the PUA requires that imputation be done on a stand-alone basis; including revenue from services other than the NAL necessarily weakens the ability the test to protect against a price squeeze; and the "broad" tests proposed by SBC do not comply with Section 13-505.1 of the PUA and Code Part 792. Joint CLEC Ex. 2.0 at 2-3. Mr. Webber also provides an extensive case history that shows that the Commission has consistently chosen to implement imputation on a stand-alone basis. *Id*., at 16-20. Although Staff did not provide this Commission imputation case history in its direct testimony, it finds such information relevant and further compelling evidence to support its position regarding the proper form of the test. Further, Staff has provided its own extensive review of prior Commission precedent as part of its statutory construction analysis in Section II of this brief. Staff IB at 42-43.

Staff noted that in defense of its own imputation tests, SBC witness Panfil aggressively argues against Staff's approach. Mr. Panfil characterizes Staff's approach as being unduly rigid, claiming that the network access line does not provide any functionality on a stand-alone basis. SBCI Ex. 1.1 at 8. As Staff witness Koch explains in direct testimony, stand-alone telephone service does provide functionality to consumers, such as access to 9-1-1 services and the ability to receive incoming calls. Staff Ex. 1.0 at 18. It is reasonable to assume such customers exist, and that is not acceptable for a price-squeeze to occur that would effectively eliminate the ability of CLECs to compete for these customers. Mr. Panfil counters this argument, as made by Mr. Koch, by claiming that he "…seems to waffle between describing imputation as being intended to protect customers and competitors." SBCI Ex. 1.1 at 14. This is clearly a misreading of Mr. Koch's testimony. Mr. Koch is in solid agreement with SBC that imputation is intended to protect the marketplace for competition. What Mr. Koch identifies as a problem is that SBC's test does not protect the market because competitors would have no incentive to provide service to low volume customers. Staff IB at 43.

Mr. Panfil also disagrees with Staff witness Mr. Koch's assertion that imputation is required for every competitive service with a unique tariffed rate. Id., at 9. Mr. Panfil provides the example of Band B usage, which has unique rates for initial and subsequent minutes, peak and off-peak rates, etc., as a counter example. Id. Here again, Mr. Panfil labors under a misunderstanding of Staff's position. The important concept that Mr. Panfil fails to comprehend is that the service must function on a stand-alone basis first, prior to the examination of whatever unique rates for the service that may exist. It is obvious that the initial minute and subsequent minutes of Band B usage do not function on a stand-alone basis. If a customer opts to select SBC as its provider of Band B usage, and chooses the *ala carte* rates for this service, they must be examined as a whole. Staff agrees that in the case of Band B usage, the entire table of applicable rates must be considered in conjunction because the individual rates cannot be offered in isolation. Staff views this similarly to the EUCL that must be purchased in addition to the retail business NAL. As explained in Mr. Koch's testimony, neither the EUCL nor the NAL can be purchased in isolation, and as such, it is appropriate to aggregate their revenue for the purpose of imputation. Staff IB at 43-44.

Staff also noted that Mr. Panfil argues that SBC's imputation test is more consistent with the FCC's approach to a price squeeze analysis than the Staff's approach. SBCI Ex. 1.1 at 13, 14. Although this may be true, it is not relevant. As has been demonstrated elsewhere in this brief, Staff's approach to imputation is the byproduct of the Illinois statute and prior decisions of the Illinois Commerce Commission. Further, the price squeeze analysis provided by Staff in this proceeding is reflective of the unique price and cost structure of SBC in Illinois. As such, any price squeeze analysis performed by the FCC in regard to rate structures outside of Illinois are simply not useful for our purposes. Staff IB at 44.

In its Reply to SBC, Staff noted that both it and the Joint CLECs argue that no level of usage, feature, and switched access revenue is appropriate for the imputation tests at issue in this proceeding. Staff RB at 44 (citations omitted). Staff and the Joint CLECs further contend that, if revenues for these services are allowed in the tests, that the averages provided by SBC are excessive and are only reflective of a minority of the marketplace. Id. SBC defends its use of averages to develop usage, feature and switched access revenues by contending that "[i]t is common practice to use averages to determine revenue levels for products and services." Id. (citations omitted). Staff noted that while this statement may be true in the context of a general representation of its revenues, it does not specifically address the practice of applying the average revenues in an imputation test, or whether the specific averages used by SBC in this proceeding are appropriate. Id.

Staff pointed out that SBC further defends the averages it uses by arguing that its business NALs would pass a broad imputation test even if 20% of the average revenues and costs for usage, features, and switched access were used. Staff RB at 44 (citations omitted). In Staff's view, this statement undermines the use of these average revenues by SBC in its imputation tests, as it illustrates just how ineffective the tests become when such averages are used. Id. This statement also fails to provide any new information. Rather, it is an alternative means of representing the same information as contained in the table on page 41 of Staff's Initial Brief. The table provided by Staff shows that there is such a significant revenue surplus in SBC's proposed imputation tests that network access lines could be reduced to zero and still pass. Staff RB at 44-45. Therefore, whether one reduces the average revenue in the test by 80% or subtracts out the cost of the network access line, the conclusion is the same -- SBC passes its own proposed imputation test even when the revenue side of the test is reduced substantially. Further, this fact does not lend itself to the conclusion that SBC's proposed tests are representative of a substantial portion of SBC's business customers, as it contends. Id. at 45. SBC is not proposing to reduce these revenue figures in the test by 80% to be more representative of its customer base. As it currently stands, the revenue proposed by SBC for its tests is representative of a minority of its customer base. Id.

Staff also pointed out that SBC, moreover, contends that "Section 13-505.1 does not require that imputation tests be performed for every customer or subgroup of customers, based on their individual purchasing patterns." Staff RB at 45 (citations omitted). While Staff finds this to be a true statement, it disagrees with the conclusion SBC attempts to draw from it. It is clear from Staff's Initial Brief and the testimony of Mr. Koch, that Staff does not propose that separate imputation tests be performed on every customer or subgroup of customers. Id. Any implication that Staff is advocating such a position is a transparent distortion of Staff's position. Nor is it Staff's understanding that the Joint CLECs or any other party is proposing such a concept. Rather, it is Staff's

understanding that an imputation test must be passed in all circumstances with no exceptions. To satisfy the statute, it is only necessary for the carrier to show that its service passes imputation under the most difficult of circumstances. For if a carrier can demonstrate that its service passes imputation under the most difficult of circumstances then logic would dictate that a service will pass imputation under all other circumstances. Id.

Staff noted that SBC makes a further attempt to justify its use of average revenues by arguing that its test results would be the same whether they were expressed on an average, per-line basis or on an aggregate basis for all its customers. Staff RB at 46. SBC appears to be confused, as this argument only addresses whether total revenue for business NAL's, usage, features, and switched access should be divided by the total number of business NAL's or not. Staff agrees with SBC that its results would be identical whether they were averaged over the total number of lines or represented as a lump sum. Id. SBC's statement is a foregone conclusion that adds nothing to the issue at hand, but rather appears to be an attempt to trivialize the matter. The issue to be addressed in Section IV (B)(2) of each party's Initial Brief, as Staff understands it, is whether SBC's inclusion of revenue for usage, features, and switched access is appropriate for the business NAL test, which is not a trivial matter. Id. SBC constructed its tests in this proceeding on a per-line basis, and as such the revenue in the test was developed on a per-line basis as well. No party to this proceeding took issue with the fact that the revenue in SBC's tests was represented on a per-line basis. Rather, parties took exception to the presence of the averages for certain services in SBC's tests, which is what Section IV (B)(2) of the brief outline is intended to address. Id.

In its Reply to CUB, Staff pointed out that the overall strategy in CUB's Initial Brief for defending its support of SBC's use of average revenues for usage, features, and switched access services would appear to be founded on a mischaracterization of various statements allegedly made by Staff witness Mr. Koch. Staff RB at 46. Mr. Koch criticized CUB witness William Dunkel's support for SBC's use of such averages in rebuttal testimony, concluding at one point that, "Implied in Mr. Dunkel's statement is that Section 13-505.1 allows for the pricing of retail services at below imputed cost for a majority of the marketplace, so long as the difference can be made up by high volume customers." Id., at 46-47 (citations omitted). CUB does not dispute the accuracy of Mr. Koch's statement. Rather, to defend its own position, CUB claims that Staff is suggesting that "any customer utilizing the UNE loop and port facilities for more features than the [sic] only the NAL and the EUCL . . . are the 'highest volume customers.'" Id. at 47 (citations omitted) CUB's characterization of Staff's position is indeed incorrect.

Staff also noted that its criticism of Mr. Dunkel was based solely on the fact that Mr. Dunkel fully supported SBC's use of average revenues for usage, features, and switched access in its imputation tests. Staff RB at 47. Data provided by SBC shows

that the average revenue used in the tests is representative of the top 34-40% of SBC's customers. Id. (citations omitted). Mr. Koch's use of the term "high volume customers" in the above quoted statement is a direct reference to this fact. Mr. Koch is not suggesting in this statement, in any manner, that any use of the loop and port to provide services above and beyond dial tone should be considered "high volume". The fact remains, however, that Mr. Dunkel and CUB support a test whose average revenue is so high that retail business NALs would pass even if the revenue of a majority of customers did not exceed imputed costs. Id.

Staff pointed out that CUB continues on to characterize Staff's tests as inappropriate for allegedly pigeonholing a "tiny group of fictional extreme customers." Staff RB at 47 (citations omitted). In supporting the concept that imputation must be passed in all circumstances, Staff is hardly being extreme. In fact, none of Staff's positions in this proceeding can credibly be characterized as extreme in that they are entirely consistent with the findings and conclusions this Commission has reached in the past. Id. (citations omitted). Staff noted that if any party's positions in this proceeding could be creditably characterized as on the extreme side it would be the CUB and SBC positions as they are requesting that this Commission abandon its past precedents. Staff is merely recommending that the Commission resolve the imputation issues at issue in this proceeding consistently with how it has treated similar issues in the past. Id. at 48.

Staff also found that CUB similarly misconstrues the Staff's responses to certain CUB data responses. Staff RB at 48 (citations omitted). CUB's entire argument here is based upon another mischaracterization of Staff's position. CUB states that Mr. Koch "*suggests* that while the average retail business revenues per line are above the imputed costs per line, the majority of the business customers have revenues that are below the imputed costs." Id. (citations omitted). Mr. Koch never said any such thing or even "suggested" it. In fact, as CUB accurately quotes Mr. Koch in the following sentence, Mr. Koch states that the tests SBC and CUB support "*allows* for the pricing of retail services at below imputed cost for a majority of the marketplace." Id. (citations omitted). This is the same point Mr. Koch and Staff have consistently made throughout this proceeding. Id. (citations omitted). Staff has repeatedly noted that because CUB's and SBC's proposed broad tests include revenues from several individually tariffed services they result in a very wide revenue surplus compared to NAL retail rates. In fact, as noted above, these margins are so wide that the access line rates could be reduced to zero and still pass an imputation test. Id. (citations omitted).

Staff also noted that CUB, following its mischaracterization of Staff's position, then uses Staff's data responses to CUB DR 1.01 in a transparently futile attempt to discredit Staff by alleging that Staff's responses to CUB DR 1.01 are inconsistent with Mr. Koch's prior testimony. Staff RB at 48-49. Staff's responses to CUB DR 1.01, however, are entirely consistent with Mr. Koch's testimony. They are, however,

inconsistent with CUB's mischaracterization of Mr. Koch's testimony. Id. at 49. For instance, after CUB mischaracterizes Mr. Koch's testimony, it claims that "However, [sic] However, in response to data requests, Mr. Koch acknowledged that it is not his testimony that the majority of business customers have averaged business revenues that are less than the imputed cost." Id. (citations omitted). It is not Mr. Koch's testimony that the majority of business customers have averaged business revenues that are less than the imputed cost; it is Mr. Koch's testimony, however, that the tests CUB and SBC support *allow* such a result. Id. Like CUB's labeling of Staff's position as "extreme," CUB's argument here that Mr. Koch "suggests" something he, in fact, does not, appears to be designed to confuse the Commission and obfuscate the paucity of CUB's entire position in this proceeding. Resorting to such transparent subterfuge should only serve to undermine CUBs position and, in turn, support Staff's positions in this proceeding. Id.

V. Rate Design Issues for Business Services Generally

A. Rate Options If Section 13-505.1 Is Deemed Not Satisfied

1. Direct Testimony

Mr. Koch notes that there are five possible alternatives to bring SBC's retail business NAL into compliance with imputation:

> Alternative 1: Restructure retail business NAL rates by creating a kind of base rate "package" for business POTS and ISDN NALs. The base rate for the NAL would increase to the point were these services pass imputation and to offset the increase, local usage and/or some central office features would be provided to customers as part of the base rates. This new "base rate package" should be developed in such a way that retail customers receive the combined services for a price equal to or lower than the rates that would be possible currently. In addition, SBCI would have to stop providing business NALs on a stand-alone basis.
>
> Staff Ex. 1.0 at 28
>
> Alternative 2: Reduce UNE loop rates in Access Area B and C.

Id.

> Alternative 3: Increase business NAL rates as in Remedy 1 but, in order to ensure that business customers "remain whole," also reduce rates for other

services so that the combined impact is revenue neutral. SBCI offers a similar proposal in this proceeding as a remedy to imputation.

Id. at 28-29

Alternative 4: Increase business NAL rates in Access Area B and C.

Id. at 29.

Alternative 5: Without providing specific direction on how to do so, require SBCI to file tariffs that would bring SBCI's retail business NAL rates into compliance with Section 13-505.1 and Code Part 792.

Id.

2. Rebuttal Testimony

Mr. Koch notes that a rate design alternative proposed by Joint CLEC witness James Webber, Joint CLEC Ex. 1.0, specifically, that SBC withdraw any service that does not pass imputation, might negatively impact customers. Staff Ex. 2.0 at 4.

3. Legal Argument in Briefs

Staff noted that, as is clear from the above, SBC's business NAL rates do not satisfy imputation. They must, accordingly, be redesigned or raised. In deciding this case, the Commission need only make the appropriate finding – that SBC's business NAL rates do not satisfy imputation under Staff's proposed narrow imputation test – and leave it to SBC to design rates in such a way that its business rates – however configured or designed – satisfy the imputation requirement. The Staff notes that the Commission can quite properly do this; there is nothing in Section 13-505.1, or in Code Part 792, that requires the Commission to do anything more than make a finding regarding whether imputation is satisfied. See 220 ILCS 5/13-505.1, 83 Ill. Admin. Code §792.10, *et seq*. (Commission need only determine whether imputation is satisfied). The Commission has reached precisely this conclusion in the past. *See* MCI Complaint Order at 32 (Lexis pagination) ("Certainly, Ameritech can implement an AAD/GID offering that results in reasonable price differences between customer classes; however Ameritech must demonstrate that the offering passes a stand alone imputation test"); GTE North Order at 155 (Lexis pagination) ("It is within the Company's discretion to pass an imputation test by reducing GTE's imputed costs, increasing end user rates, or by some combination thereof."). Staff IB at 45 (some citations omitted).

Staff also pointed out, moreover, that SBC is in possession of the information necessary to design compliant rates. Staff IB at 45. The Commission can (and should) therefore, quite properly place the onus upon SBC to find an appropriate solution. In this regard, there are several options, of which the following list is certainly not exhaustive. Id.

Staff noted that there are several ways that SBC's business NAL rates can be made to satisfy the imputation requirement. These include, but are not necessarily limited to, the alternatives discussed in Mr. Koch's testimony.

Staff noted that first, SBC might restructure retail business NAL rates by creating a kind of base rate "package" for business POTS and ISDN NALs. Staff IB at 46 (citations omitted). Under this proposal, SBC would raise the base rate for the NAL to the point where these services pass imputation. Id. To offset this increase in price, SBC would provide customers with local usage and/or some central office features as part of the base rates. Id. Ideally, this new "base rate package" should be developed in such a way that retail customers receive the combined services for a price equal to or lower than the rates that would be possible currently. Staff thought that if SBC elects to adopt this solution, it must cease providing business NALs on a stand-alone basis. Id. As noted above, without more, the stand-alone NAL does not pass imputation. Id.

Staff points out, however, that care should be taken not to confuse this potential rate design alternative with the Joint CLECs' proposal that SBC might cease providing retail business service altogether. Joint CLEC Ex. 1.0 at 49-50. Under the alternative to which Staff refers, SBC would continue to offer competitive business service, but would not offer the business NAL on a stand-alone basis. Staff IB at 46.

As a second alternative, Staff noted that SBC might reduce its UNE loop rates in all access areas. Were SBC to adopt this approach, the imputation problem would be quickly and easily solved, however this would be inconsistent with the Commission's Order in Docket 02-0864. Staff IB at 47 (citations omitted).

Staff pointed out that the Commission determined, only five months ago, and after an extended and hotly contested proceeding, that SBC's UNE loop rates were in fact too low, and permitted SBC to raise them. Staff IB at 47 (citations omitted). The Commission made this decision based in part upon its conclusion that SBC's costs for provisioning the UNE loop had increased. Id. Indeed, this proceeding is convened solely for the purpose of determining how to deal with imputation questions caused by those very UNE loop increases. Id.

Moreover, Staff pointed out that under Section 252(d)(2)(A) of the federal Telecommunications Act, SBC is entitled to recover the costs it incurs in providing UNEs, including the UNE loop, to other telecommunications carriers. Staff IB at 47

(citations omitted). To the extent that the Commission determines – as it has, in the *UNE Loop Order* – that SBC's costs for providing the UNE loop have increased, it cannot, without inviting a conflict with federal law, reduce SBC's UNE loop rates – which are, after all cost based – for the purpose of bringing those rates into compliance with a state law imputation requirement. Id.

Staff noted that the Joint CLECs propose a solution very similar to reducing UNE rates: specifically, that, where SBC's imputed cost for a service exceeds the associated revenue for that service, the Commission should direct SBC to credit CLECs with the difference. Staff IB at 47 (citations omitted). It should be noted that this proposal has all of the legal and practical problems described above, as well as potentially violating the filed rate doctrine, which renders it unlawful for public utilities, and telecommunications carriers providing non-competitive services to: "refund or remit, directly or indirectly, in any manner or by any device, any portion of the rates or other charges so specified, nor extend to any corporation or person any form of contract or agreement or any rule or regulation or any facility or privilege except such as are regularly and uniformly extended to all corporations and persons." Id., at 47-48 (citations omitted).

Staff opined that there are other flaws inherent in the Joint CLECs' proposal. First, it would unnecessarily complicate the rate structure, making it very difficult to determine what UNE loop rates actually would be, since they could not be determined by reference to the tariff – the traditional way to determine what rates are. Staff IB at 48 (citations omitted). Second, issuance of rebates or refunds – however characterized – begin to have the look and feel of subsidies, something the Commission has long opposed. Id.

Staff noted that under the third alternative SBC might increase its retail business NAL rates in the manner proposed above, but, in order to ensure that business customers "remain whole," also reduce rates for other services so that the combined impact is revenue neutral. Staff IB at 48 (citations omitted). SBC notes the existence of a similar rate design alternative.

Staff pointed out, however, that while such a proposal would, if adopted, be revenue-neutral to SBC, it would not be revenue-neutral as to individual customers. Staff IB at 48-49 (citations omitted). It would result in certain users paying increased rates. Specifically, those customers who make few calls and subscribe to no vertical services would pay relatively more for service, while those customers who make a larger number of calls and subscribe to vertical services would pay relatively less. Staff IB at 49.

Staff noted that a fourth rate design alternative would be for SBC to raise its retail business NAL rates in those access areas, and for those access line types, which do

not satisfy imputation. A key difficulty with this alternative is the fact that Section 13-502.5(b) of the Public Utilities Act caps rates for certain business customers. Staff IB at 49 (citations omitted). The Staff recommends that the Commission order SBC to file rates for business NAL rates designed in such a way as to satisfy imputation and all other applicable laws by a date certain after entry of its Order in this proceeding. Id.

In its Reply Brief, Staff reaffirms its commitment to the proposition that "[t]he Commission can (and should) … quite properly place the onus upon SBC to find an appropriate solution [to the imputation problem]." Staff RB at 49. First, the Commission has done precisely this in the past. Id. Second, neither Section 13-505.1 nor the Commission's Rules require more than this. Third, SBC's Petition in this proceeding may foreclose other options. Id.

Staff noted that SBC filed a *Petition* in this proceeding seeking, *inter alia*, a Commission Order concluding that "[SBC's] standard retail access lines rates and ISDN rates satisfy the requirements of Section 13-505.1, and provide [SBC] with direction with respect to COPTS rates." Staff RB at 49-50 (citations omitted). In other words, SBC has *not* requested that the Commission's Order in this proceeding address rate design questions other than those associated with COPTS rates. Id., at 50.

Staff found this significant, since the courts have found in several cases that the Commission cannot grant relief that a petitioner or complainant does not request. Staff RB at 50, *citing* Peoples Gas v. Commerce Comm'n, 221 Ill. App.3d 1053, 1059; 583 N.E.2d 68, 71; 164 Ill. Dec. 514; 1991 Ill. App. Lexis 1906 at 12 (1st Dist. 1991); City of Champaign v. Commerce Comm'n, 141 Ill. App.3d 457, 461; 490 N.E.2d 119, 122; 95 Ill. Dec. 646; 1986 Ill. App. Lexis 1929 at 8-10 (4th Dist. 1986). The Commission recognizes this proposition, in which SBC appears to concur fully. *See Order* at 29, Illinois Commerce Commission On Its Own Motion -vs- Illinois Bell Telephone Company: Investigation of the propriety of the rates, terms, and conditions related to the provision of the Basic COPTS Port and the COPTS-Coin Line Port, ICC Docket No. 01-0609, 2003 Ill. PUC Lexis 821 at 75-76 (October 22, 2003)(" We begin first by [agreeing] with SBC that the scope of this docket is indeed limited by the Petitions filed by Data Net Systems, LLC, TruComm Corporation, and Payphone Services, Inc. and the Commission's Initiating Order"). Accordingly, the Commission may not be in a position to direct a specific rate design here. Id.

That said, the parties have made a number of rate design proposals. SBC notes the existence of a number of rate design options, chiefly in support of its assertions that none other than raising business NAL rates are reasonable or workable. Staff RB at 50-51 (citations omitted). SBC first states that it has no intention of reducing its UNE loop rates, thereby effectively removing this option from consideration. Id., at 51 (citations omitted). SBC further argues that it should not be required to discontinue providing the

business NAL on a stand-alone basis, since it contends that its customers want to purchase this service. Id.

Staff also noted that SBC contends that the increases in the business NAL rate required to satisfy the imputation requirement would be "relatively modest" and "reasonable in the marketplace". Staff RB at 51 (citations omitted). SBC prefers this alternative to what it refers to as "revenue neutral" solutions, which is the term it uses to describe rate design alternatives that include the business NAL, and some combination of usage, vertical services, and other features. Id. SBC appears to consider these options essentially anti-competitive, or at least unnecessary to promote competition. Id. In raising these points, SBC attempts to rehabilitate its contention that its so called "broad" imputation test is proper, by asserting that CLECs can compete for low-margin customers, simply by using high-margin customers to subsidize them. Id. Staff has already pointed out the defects in the latter argument. However, the Staff notes that SBC's proposal to increase the business NAL rate is lawful. Id.

B. Implementation Issues: the Under 4-Line Rate Cap in Section 13-502.5

1. Direct Testimony

2. Rebuttal Testimony

3. Legal Argument in Briefs

Staff noted that the prospective solutions for the failure of SBC's business NAL to satisfy imputation must be considered in light of Section 13-502.5. Staff IB at 50. To the extent that SBC's rates for business NAL services provided to retail business end users with four or fewer access lines are capped at their May 1, 2001 levels, implementation of some of the options above will be problematic. Indeed, SBC raises precisely such contentions, suggesting that its billing systems would have to be extensively revamped to differentiate between customers subject to, or not subject to, the four or fewer access line rate cap. Id. (citations omitted). SBC accordingly suggests deferring any rate changes to July 1, 2005.

Staff pointed out that the General Assembly enacted Section 13-502.5 in June of 2001. *See* P.A. 92-22 (effective date of July 1, 2001). Accordingly, although SBC has had over three years to accommodate its billing systems to the existence of a legally mandated class of small business customers, it apparently has not done so. Its failure to do so cannot now serve as a basis for permitting it to violate imputation. Deferring resolution of this issue prejudices the CLECs that are placed at a competitive disadvantage for a period of something like half a year. The Commission should therefore disregard SBC's recommendation that the Commission should wait to July 1, 2005 to resolve this matter. Staff IB at 50-51.

Staff also noted that it might also be argued that the statutory imputation requirement conflicts with Section 13-502.5, since Section 13-502.5 caps certain rates, thereby arguably preventing SBC from bringing these rates into line with imputation. This argument is untenable, at least with respect to the application of certain of the possible alternatives the Commission has available to it. Staff IB at 51.

Staff provided the following illustration; Section 13-502.5 provides that: "Rates for retail telecommunications services provided to business end users with 4 or fewer access lines shall not exceed the rates the carrier charged for those services on May 1, 2001[.]" Staff IB at 51 (citations omitted). However, to the extent that SBC ceases to offer the business NAL on a stand-alone basis, this provision need not be implicated, since nothing in Section 13-502.5 prohibits discontinuing a service offering. Likewise, if a package of services is offered, consistent with the alternative noted by Staff above, such a package could be designed in such a way that the total package both passes imputation, and does not constitute an increase from the rates in effect on May 1, 2001. Again, it must be stressed that SBC, and no other party, is responsible for designing rates in such a way that they comply with all applicable laws. Id.

Staff pointed out that the Section 13-502.5 rate cap provision is not as much in conflict with the statutorily mandated imputation requirements as it simply limits the options available to SBC in finding a solution. Staff IB at 51. SBC's failure to implement billing systems capable of differentiating between two legally mandated classes of business customers further hinders this effort. SBC is barred from raising the retail rates that it charges business customers with 4 or fewer access lines until July 1, 2005. By extension, because SBC's billing system is not able to distinguish between customers, this further calls into question SBC's ability to implement any sort of retail rate increase without violating the 13-502.5 rate cap. Staff IB at 51-52. It appears that SBC is not in a position, based on its own testimony, to increase stand-alone business NAL rates, since it is unable to distinguish between customers with four or fewer access lines, and those with five or more, and therefore unable to ensure that stand-alone business NAL rates will not increase for the former group. However, this problem is SBC's to solve; the Commission need only determine that SBC has not satisfied imputation. Staff IB at 52.

In its Reply Brief, Staff again emphasized that the prospective solutions for the failure of SBC's business NAL to satisfy imputation must be considered in the rate cap for services provide to small business customers in Section 13-502.5 of the Act, which caps such rates at their May 1, 2001 levels through July 1, 2005. Staff RB at 51. Thus, implementation of some of the rate design options floated in this proceeding will be difficult. SBC raises precisely such contentions, suggesting that its billing systems would have to be extensively revamped to differentiate between customers subject to, or not

subject to, the four or fewer access line rate cap. Id., at 51-52 (citations omitted). SBC accordingly suggests deferring any rate changes to July 1, 2005. Id., at 52.

Staff urged the Commission to decline to do so. Staff RB at 52. The General Assembly enacted Section 13-502.5 3 ½ years ago; accordingly, although SBC has had ample time to accommodate its billing systems to the existence of a legally mandated class of small business customers, it apparently has not done so. Its failure to do so cannot now serve as a basis for permitting it to violate imputation. Deferring resolution of this issue prejudices the CLECs that are placed at a competitive disadvantage for a period of something like half a year. Id.

Staff noted that the Section 13-502.5 rate cap provision is not as much in conflict with the statutorily mandated imputation requirements as it simply limits the options available to SBC in finding a solution. Staff RB at 52. SBC's failure to implement billing systems capable of differentiating between two legally mandated classes of business customers further hinders this effort. SBC is barred from raising the retail rates that it charges business customers with 4 or fewer access lines until July 1, 2005. Id. By extension, because SBC's billing system is not able to distinguish between customers, this further calls into question SBC's ability to implement any sort of retail rate increase without violating the 13-502.5 rate cap. Id. It appears that SBC is not in a position, based on its own testimony, to increase stand-alone business NAL rates, since it is unable to distinguish between customers with four or fewer access lines, and those with five or more, and therefore unable to ensure that stand-alone business NAL rates will not increase for the former group. However, this problem is SBC's to solve; the Commission need only determine that SBC has not satisfied imputation. Id.

Staff pointed out that the Joint CLECs state that they do "not recommend[] that the Commission direct SBC to, for example, raise specific retail bu siness rates or reduce specific UNE prices or other wholesale service prices to achieve compliance [with imputation.]" Staff RB at 53 (citations omitted). Indeed, the Joint CLECs do not recommend that the Commission direct SBC to take any specific step. Id. It is the Joint CLECs' position that "SBC should be responsible for developing and implementing an overall plan to achieve compliance with imputation requirements[.]" Id. (citations omitted).

Staff noted that the Joint CLECs nonetheless propose four options that SBC might utilize to pass imputation. Staff RB at 53 (citations omitted). Specifically, the Joint CLECs observe that, to comply with imputation, SBC might: (1) voluntarily reduce UNE loop rates; (2) provide credits to CLECs in the amount by which SBC's UNE loop rates fail imputation; (3) withdraw those services that fail imputation; or (4) raise retail business NAL rates. Staff RB at 53 (citations omitted). Staff noted that the Joint CLECs' first option, a reduction in UNE loop rates, appears to have been overtaken by events. As the Joint CLECs and Staff both observed in their respective Initial Briefs,

SBC would have to do this of its own volition. Staff RB at 53 (citations omitted). It is now clear, to the extent that it ever was *unclear*, that SBC has no intention of undertaking this course. Id., *citing* SBC IB at 26 ("SBC Illinois is not willing to reduce its UNE loop rates on a voluntary basis"). Accordingly, further consideration of this option appears unwarranted.

Staff pointed out that the Joint CLECs appear to conclude that, whatever steps SBC takes to bring its retail business NAL rates into compliance with imputation, it should do so very promptly indeed. Staff RB at 53. The Joint CLECs recommend that the Commission order SBC to file a "report and plan of action" that describes how SBC proposes to comply with imputation, accompanied by new imputation studies, no later than 21 days after the Commission enters its Order in this proceeding. Staff RB at 53-54 (citations omitted). Further, the Joint CLECs aver, SBC should be required to implement its recommended solutions within 35 days of the Commission Order. Id.

Staff also pointed out that the Department of Defense and other Federal Executive Agencies (hereafter "DOD/FEA") is, in essence, the federal government, and, as such, it uses, and therefore purchases, an extraordinarily large volume of telecommunications services in Illinois (as presumably elsewhere). Staff RB at 54 (citations omitted). The DOD/FEA therefore asserts that it is likely to be significantly affected by whatever the Commission ultimately orders in this proceeding. Id. The DOD/FEA recommends that the Commission order SBC to "make the minimum necessary increases in the retail line charges for Access Areas B and C, with compensating reductions in the charges for other services to business end users, so that the impact on business users [is] revenue neutral overall." Id. (citations omitted). To the extent that the Commission is inclined to adopt any of the options proposed by the Staff, DOD/FEA advocates adoption of the third, or "make-whole" realignment. Id. DOD/FEA opposes, as "too amorphous", the proposal that SBC be required to resolve the imputation problem itself, unless the Commission gives "additional clarification", or imposes "more constraints" upon SBC. Id.

While the Staff is sympathetic to DOD/FEA's position in this proceeding – DOD/FEA appears to be the entity that has the most at stake as a result of any order the Commission enters – the fact remains that the scope of the SBC petition, the statute, the rules, and prior Commission decisions all militate against the Commission doing anything in this proceeding but finding that SBC's business NAL rate does not pass imputation, and directing SBC to fix the problem. Staff RB at 54-55.

The Staff recommends that the Commission (1) find that SBC's business NAL rate fails to satisfy imputation; and (2) direct SBC to file rates in whatever form that satisfy imputation. Staff RB at 55. The Staff is uncertain regarding whether the Joint CLECs' rather stringent timetables for compliance can reasonably be met. Staff

recommends that the Commission order SBC to comply within 45 days of the final Order in this proceeding. Id.

VI. Payphone Issues

A. Interrelationship with Docket No. 98-0195

1. Direct Testimony

In his direct testimony, Mr. Koch stated that rates for COPTS (coin operated pay telephone service had been set by the Commission in its Payphone Order, using the federally mandated New Services Test. Staff Ex. 1.0 at 30. He further noted that, when the Commission, in its UNE Loop Order, authorized SBC to recover higher TELRICs for UNE loops, this increase, combined with the fact that the LRSICs, upon which SBC's COPTS rates are based, were not simultaneously updated, has the effect of causing SBC COPTS rates to fail imputation. Id.

2. Rebuttal Testimony

Mr. Koch did not address this issue in his rebuttal testimony. See Staff Ex. 2.0.

3. Legal Argument in Briefs

Staff noted that Independent payphone providers (hereafter "IPPs") purchase access to the telecommunications network from SBC as the ILEC, and resell that network access to the public through public payphones. Staff IB at 52, *citing Interim Order* at 2, Illinois Commerce Commission On its Own Motion: Investigation Into Certain Payphone Issues as Directed in Docket 97-0225, ICC Docket No. 98-0195 (November 12, 2003) (hereafter "Payphone Order"). IPPs are considered retail business customers rather than telecommunications carriers. *First Report And Order*, ¶876, In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers, FCC No. 96-325, CC Docket No. 96-98; CC Docket No. 95-185, 11 FCC Rcd 15499; 1996 FCC LEXIS 4312; 4 Comm. Reg. (P & F) 1 (August 8, 1996) (hereafter "Local Competition Order"); SBC Ex. 1.0 at 32, *et seq*. Accordingly, SBC must submit, and in fact has submitted, imputation studies for its COPTS ("coin-operated pay telephone service"). Staff RB at 52-53 (citations omitted).

Staff explained, however, that it is vital to understand that network services rates ILECs charge to IPPS must satisfy certain federal requirements. As part of the Telecommunications Act of 1996, Congress enacted Section 276, entitled "Provision of

Payphone Service". Staff RB at 53 (citations omitted). Pursuant to subsection (b)(1)(C) of Section 276, the FCC directed the use of the existing New Services Test under the authority of Section 276 of TA '96. Id., at 54 *citing Report and Order*, In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 / Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, FCC No. 96-388, CC Docket No. 96-128; CC Docket. No. 91-35, 11 FCC Rcd 20541; 1996 FCC LEXIS 5261; 4 Comm. Reg. (P & F) 938 (September 20, 1996) (hereafter "FCC Payphone Order"); *Order On Reconsideration,* In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 / Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, FCC No. 96-439, CC Docket Nos. 96-128, 91-35, and 96-439, 11 FCC Rcd 21233; 1996 FCC Lexis 6257; 5 Comm. Reg. (P & F) 321 (November 8, 1996) (hereafter, "FCC Payphone Order on Reconsideration"). In the *FCC Payphone Order*, that agency determined that the existing new services test should be applied to ILEC payphone operations to insure that Section 276(a) was satisfied. FCC Payphone Order, ¶146; FCC Payphone Order on Reconsideration, ¶163, and n. 492. The New Services Test is codified as 47 C.F.R. 61.49(g). FCC Payphone Order on Reconsideration, ¶163, n. 492. Staff IB at 54-55.

Staff explained that the New Services Test is essentially a mechanism that imposes a cost-based price ceiling on certain ILEC services. Staff RB at 55 (citations omitted). This Commission has determined that, to comply with Section 276(a), SBC's rates for services provided to IPPs must satisfy both the New Services test, and imputation requirements. Payphone Order at 11, 20. In its *Payphone Order*, the Commission found that, when an ILEC's payphone rates pass the imputation test established in Code Part 792, it satisfies the anti-subsidy requirements of Section 276. Payphone Order at 6, 11. Likewise, the Commission determined that, since the purpose of the New Services Test is to establish a price ceiling on the services that an ILEC charges to IPPs, an ILEC complies with the anti-discrimination provisions of Section 276 when its payphone rates satisfy the Cost of Service rules the Commission established in Code Part 791 (LRSIC), with an overhead allocation added. Payphone Order at 37. Applying these principles, the Commission found that SBC's then-effective rates did not satisfy the New Services Test, and directed the company to file revised tariffs. Id. at 35. The Commission determined that SBC's then-effective rates satisfied imputation. Staff IB at 55.

Staff noted that the Commission's decision to permit SBC to raise its UNE loop rates, which, obviously, the Commission made subsequent to entry of its *Payphone Order*, has the effect of causing the COPTS rates SBC charges independent payphone providers for network access to fail imputation in all but one access area. Staff RB at 56 (citations omitted). However, it is also the case that these COPTS rates are set – at

least in broad outline – under federal guidelines. The question is, then, to what, if any, extent imputation requirements conflict with these federal guidelines. Id.

B. Preemption

1. Direct Testimony

Mr. Koch did not address this issue in his direct testimony. See Staff Ex. 1.0.

2. Rebuttal Testimony

Mr. Koch did not address this issue in his rebuttal testimony. See Staff Ex. 2.0.

3. Legal Argument in Briefs

Staff opined that, facially, at least, the question of preemption is in this case fairly clear. Section 276(c) of the federal Act provides, as noted above, that: "To the extent that any State requirements are inconsistent with the Commission's regulations [promulgated under Section 276, and including 47 C.F.R. §61.49(g)], the Commission's regulations on such matters shall preempt such State requirements[.]" Staff IB at 56 (citations omitted). However, a closer analysis reveals that this is of little utility in resolving the preemption question.

Staff reasoned that as Section 276 requires that ILEC payphone rates be set in such a manner as to be non-discriminatory, and to not subsidize the ILEC's own payphone operations; however, the Congress left to the FCC the specifics of how to implement these requirements, authorizing the FCC to make rules that establish non-structural safeguards to assure compliance with Section 276(a). The FCC accomplished this by applying the New Services Test, 47 C.F.R. §61.49(g), to ILEC payphone operations. Staff IB at 56 (citations omitted).

Staff noted, however, that Section 61.49(g) does not, in and of itself, contain substantive requirements regarding how to implement the New Services Test. This regulation, then, is obviously a requirement that filings take a certain prescribed form, a conclusion confirmed by the title of Section 61.49 – "Supporting information to be submitted with letters of transmittal for tariffs of carriers subject to price cap regulation." It is clear that the FCC required such filings so that the agency reviewing the filing (in this case, a state Commission) has information sufficient to determine whether the rates in question are cost based, consistent with the requirements of Section 276 with regard to the removal of subsidies from exchange and exchange access services, and nondiscriminatory. Clearly, Section 61.49(g) does not impose *substantive* requirements. Staff IB at 57-58 (citations omitted).

While the FCC has subsequently given state Commissions some additional guidance regarding how to implement ILEC tariffs that satisfy the New Services Test (see FCC Payphone Order on Reconsideration, ¶163), this guidance has been modest, as can be seen from the FCC's adoption of its *Order*, In the Matter of Wisconsin Public Service Commission: Order Directing Filings, FCC No. 02-25; CPD 00-01 (January 31, 2002) (hereafter "WPSC Order"). In that *Order*, the FCC determined that : "States may continue to use UNE loading factors to evaluate BOCs' overhead allocation for payphone services, but we do not require that UNE overhead allocations must serve as a ceiling on payphone service overhead loading." WPSC Order, ¶58. Staff IB at 59.

In sum, the Staff noted that the FCC has determined that state Commissions are to oversee implementation of Section 276(a). *See* FCC Payphone Order on Reconsideration, ¶163 (ILECs are to file intrastate tariffs, to be reviewed by state Commissions). The FCC requires states to use, as one vehicle for accomplishing this end, the New Services Test, which is, as seen, a price cap requirement, with which ILECs must demonstrate compliance through filings that include certain information in a prescribed form. States, in turn, must evaluate ILEC payphone tariffs thus filed to make certain that COPTS rates are cost based, consistent with the requirements of Section 276 with regard to the removal of subsidies from exchange and exchange access services, and nondiscriminatory. To the extent a state regulation does not impede these requirements, it is difficult to see how such a regulation would be preempted. Staff IB at 59.

Staff noted that while it would appear at first blush that the Illinois requirement that SBC's payphone rates pass imputation conflicts with Section 276 to the extent that it requires an increase in such rates above federally-mandated levels, this is simply not the case. In its *Payphone Order*, this Commission did not so much *set* payphone rates as *establish a methodology* by which such rates properly are set. *See* Payphone Order at 37 (Commission establishes methodology to yield reasonable, Section 276-compliant payphone rates). Staff IB at 59-60.

Staff emphasized that this is an important point. The FCC has required ILECs to tariff, and the state Commissions to implement, among other things, "cost based" rates. Payphone Order on Reconsideration, ¶163. It stands to reason that an ILEC's cost structure can, from time to time, change. Indeed, the Commission determined, in its *SBC UNE Loop Order*, that SBC's TELRIC costs associated with providing the loop on an unbundled basis has increased over time. *See, generally, Order*, Illinois Bell Telephone Company: Filing to increase Unbundled Loop and Nonrecurring Rates, ICC Docket No. 02-0864, 2002 Ill. PUC Lexis 564 (June 9, 2004). Thus, it stands to reason that, as SBC's costs associated with COPTS access increase, of which the loop comprises a substantial portion, COPTs rates ought to increase as well. In short, the Commission need not and should not assume that the rates established as a result of its *Payphone Order* are set in stone. If – as is the case – SBC's COPTS rates do not

satisfy imputation, then they should increase, or should be redesigned, notwithstanding the recency of the *Payphone Order*. Staff IB at 60.

Consequently, Staff concluded that it becomes clear that there is no preemption question here. The Commission can devise a solution in which SBC's COPTS rates satisfy *both* Section 276 requirements *and* imputation. Id.

Staff noted that the IPTA appears to suggest that Section 276 preempts further Commission action regarding payphone rates. IPTA Ex. 1.0 at 8-9. As noted above, however, what Section 276 preempts is any state law, regulation or rule that mandates payphone rates which (1) are discriminatory; (2) are not cost-based; or (3) subsidize the ILEC's own payphone service. A reevaluation of payphone rates, based on new cost information, and conducted according to the methodology established by the Commission in its *Payphone Order*, would very clearly *not* constitute such a law, regulation, or rule. Indeed, to the extent that SBC's COPTs rates no longer pass imputation, such rates are arguably not cost-based as required by Section 276. Staff IB at 60-61.

Staff found that the IPTA makes much of the fact that the Commission issued its *Payphone Order* over six years after the IPTA filed its Petition. IPTA Ex. 1.0 at 5, 6. This, it suggests, has worked a major hardship on IPPs, as they were compelled during that period to pay "excessive payphone access rates that were not in compliance with the Federal requirements[.]" Id. at 5. The IPTA suggests that the fact that it and its members "were compelled to pour significant resources into [the ICC] investigation" leading to COPTS rates somehow prevents the Commission from reviewing the rates in question in the light of new information. Staff IB at 61.

However, as the Commission noted in the *Payphone Order*, the alleged delay in resolution of the proceeding was attributable in large part to IPTA's desultory pursuit of its claim; by way of example, IPTA filed its Direct Testimony in the *Payphone Proceeding* nearly six months late. Payphone Order at 43, n.16. Staff IB at 61.

Accordingly, Staff pointed out that the IPTA's claim that it is somehow hard done by should fall on deaf ears. The IPTA's members paid lawful, tariffed rates at all relevant times, and indeed those rates were, as the Commission noted, characterized by "deep discounts". Moreover, even if this were not the case, the IPTA cannot be heard to argue that the Commission has no authority to revisit its past rate decisions. Staff IB at 62 (citations omitted).

In summary, Staff noted that IPTA seeks to maintain rates for its members at a level far more advantageous than those available to any other retail business customer. There is no public policy basis for such treatment, and, as noted above, it would violate state law. The IPTA's arguments should therefore be discounted. Staff IB at 62.

The Staff explained that it does not suggest that the Commission erred in its *Payphone Order*. To the contrary, the Commission adopted a correct methodology for payphone services imputation, application of the New Services Test, and application of the proper overhead loading factor. Moreover, based upon the cost information available in that proceeding, the Commission ordered implementation of the proper rates. Further, the Commission established a methodology that can be utilized to reset COPTS rates at such time as a change in circumstances warrants it. Specifically, these rates are to be calculated using the LRSIC for the service as well as an allocation of common overheads based on UNE overhead factors. Staff IB at 62.

Finally, the Staff pointed out that there has been a change in circumstances since the entry of the *Payphone Order*. Specifically, the Commission has approved a change in SBC's methodology for determining UNE loop rates, which includes UNE loop costs for COPTS lines. *See, generally,* SBC UNE Loop Order. Although the change in methodology is for UNE loop rate calculations, it is significant in that the methodology also affects the retail COPTS rate calculations. Namely, the Commission approved a change in the cost model by which SBC calculates its UNE loop costs. The new model, LoopCAT, is not yet currently being used by SBC to calculate the LRSIC for retail COPTS lines, but the company concedes that it should do so on a going forward basis. In as much as the LRSIC for COPTS services needs to be updated to reflect the adoption of the new cost model, the retail rate for COPTS will be affected. Second, SBC's UNE overhead factor was modified as a result of the Order. As was indicated above, the UNE overhead factor is a component of the COPTS rate calculation methodology for SBC's payphone rates. Accordingly, the Commission can, if it sees fit to do so, quite properly reset SBC's COPTS rates, such that they satisfy the imputation requirement. Staff IB at 63.

In its Reply Brief, Staff pointed out that the IPTA argues that COPTS rates the Commission set for SBC in the *Payphone Order* are "conclusively established" are "the only permissible rates[,]"and "must be applied to network services provided to payphone providers[,]"and cannot be linked or compared to retail business rates. Staff RB at 55 (citations omitted). IPTA's position is based upon the position – undeniably true – that "[i]t is beyond per adventure [sic] that network access rates to payphone providers must be cost based in compliance with the New Services Test." IPTA IB at 15. This uncontroversial assertion is virtually the only correct one that IPTA makes, however. Staff RB at 55.

Staff noted that IPTA appears to contend that any alteration in this proceeding, or indeed resulting from this proceeding, of the rates set in the *Payphone Order* is (1) preempted by Section 276(c) of the federal Telecommunications Act of 1996; (2) the equivalent of an improper collateral attack upon the *Payphone Order*; and (3) in any

case, unsupported by substantial evidence. Staff RB at 56 (citations omitted). These assertions are incorrect.

The Staff noted that although it dealt extensively with the alleged preemption question in its Initial Brief and accordingly will not recapitulate such arguments at length here, however, one of IPTA's arguments is sufficiently inexplicable to warrant examination. Staff pointed out that IPTA takes the curious position that: "The Commission has determined [proper COPTS] rates in Docket No. 98-0195 [the Payphone Order]. Application of state regulatory requirements establishing a different basis for those rates have [sic] been expressly preempted by the FCC." Staff RB at 56, citing IPTA IB at 5.

Thus, IPTA appears to argue that, to the extent that application of the imputation requirement requires any *change* in existing COPTS rates, its application is therefore preempted. Staff RB at 56 (citations omitted).

If the Staff correctly interprets this rather opaque contention, the IPTA is arguing that, where the Commission has adopted Section 276-compliant COPTS rates, Section 276 preempts adoption of Section 276-compliant COPTS rates in *other subsequent* proceedings based on changed costs. Staff RB at 56. This simply cannot be true; it is tantamount to arguing that cost-based rates do not change as costs change, which would, of course, render the term "cost-based" meaningless, presumably an outcome IPTA would find deplorable.

Further, as Staff noted in its *Initial Brief*, it is not the case that Section 276 preempts imputation; the imputation requirement and FCC rules adopted under Section 276 can, and readily do, coexist. Section 276 requires payphone rates that are non-discriminatory, cost based, and that do not subsidize other ILEC operations. 47 U.S.C. §276(a); *Order On Reconsideration,* ¶163, In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 / Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, FCC No. 96-439, CC Docket Nos. 96-128, 91-35, and 96-439, 11 FCC Rcd 21233; 1996 FCC Lexis 6257; 5 Comm. Reg. (P & F) 321 (November 8, 1996) (hereafter, "FCC Payphone Order on Reconsideration"); Staff IB at 56, *et seq*. It stands to reason that, since these are the requirements, Section 276 preempts only those state requirements that mandate COPTS rates that are discriminatory, not cost based, or that subsidize ILEC operations. *See* Staff IB at 60-61 ("Section 276 preempts … any state law, regulation or rule that mandates payphone rates which (1) are discriminatory; (2) are not cost-based; or (3) subsidize the ILEC's own payphone service"). It follows from this that a reevaluation of payphone rates, based on new cost information, and conducted according to the methodology established by the Commission in its *Payphone Order*, would very clearly *not* constitute a state requirement inconsistent with Section 276; indeed, as noted above, the FCC has found

that Section 276 requires "cost-based rates". FCC Payphone Order On Reconsideration, ¶163. Thus, it cannot be argued that a state law requiring rates to be cost based – as imputation does – could possibly constitute a "State requirement[] … inconsistent with the [FCC]'s regulations" in violation of Section 276(c); it appears to the Staff that imputation is a state requirement *absolutely consistent* with FCC rules promulgated under Section 276. Staff RB at 57-58.

Indeed the Commission found that the imputation test is a necessary tool so that an ILEC's COPTS does not subsidize its other operations. *See* Payphone Order at 7 ("The [imputation] test is intended to guard against cross-subsidization of competitive services by non-competitive services"). IPTA cannot, and does not, dispute this. Accordingly, the Commission should dismiss out of hand IPTA's arguments regarding the application of the imputation test to COPTS rates. Staff RB at 57-58.

IPTA next argues that the application of an imputation requirement constitutes an improper collateral attack on the Commission's *Payphone Order*. IPTA IB at 7-13. This line of argument is chiefly directed at SBC, but certain aspects of it warrant discussion by Staff. Staff RB at 58.

As the Staff noted in its *Initial Brief*, the Commission adopted, in its *Payphone Order*, a methodology whereby COPTS rates will be set going forward. Staff IB at 62. It further adopted proper rates based on then-existing cost information. Id. Requiring such rates to satisfy imputation – as required by state law – does not constitute a collateral attack on this methodology. Instead, it is nothing more than recognition of the changed cost basis of these rates. Indeed, as the Staff demonstrated in its *Initial Brief*, SBC can file COPTS rates that satisfy imputation by the very simple and straightforward expedient of: (1) developing updated LRSIC costs, modeled by the LoopCAT model, which the Commission approved in the *UNE Loop Order*; and (2) applying the revised UNE overhead loading to those costs, thereby yielding a rate. Staff IB at 63. This methodology is precisely the one the Commission prescribed in its *Payphone Order*. Payphone Order at 37. Staff RB at 58.

Staff found that IPTA utterly fails to appreciate that the Commission did not, in the *Payphone Order*, set COPTS rates that SBC is *required* to charge from now until the last trumpet is sounded. In the *Payphone Proceeding*, the Commission evaluated the methodology by which SBC set its COPTS rates, for the purpose of determining whether that methodology satisfied Section 276 and associated FCC rules. The Commission directed the adoption of a methodology, not the adoption of specific rates, just as the FCC rules require state Commissions to evaluate ILEC COPTS rates based on whether those rates were derived using an acceptable methodology, rather that whether the rates were too high compared to some arbitrary benchmark. Accordingly, IPTA's assertion that application of the imputation requirement constitutes an improper

collateral attack upon the *Payphone Order* must be rejected. It is no such thing. Staff RB at 59.

IPTA further argues, in a somewhat related vein, that evidence has not been adduced in this proceeding such as would warrant revision of COPTS rates. IPTA IB at 5, *et seq*. IPTA contends that "any changes to [COPTS] rates [based] on the completely [sic] dearth of evidence in the instant docket would be arbitrary and capricious." Id. at 5. IPTA asserts that "[t]he Docket No. 98-0195 proceedings [upon which the Commission based the Payphone Order] involved scores of testimonies filed in two complete sets of hearings." Id. at 6. Accordingly, IPTA contends that the matter of COPTS rates ought not to be revisited here. Staff RB at 59.

Staff found one very significant flaw in this theory. Specifically, it assumes that there is somehow no evidentiary support for increased costs. This assertion, however, is incorrect, and in fact incorrect to an extreme degree. Staff RB at 59.

Staff notes that IPTA was a party to the *UNE Loop Proceeding*. Accordingly, it is, or should be, aware of the fact that the Commission set SBC's UNE loop rates after a vigorously contested proceeding in which numerous parties participated, a very large number of witnesses offered testimony[1], and a considerable volume of additional evidence was adduced. *See, generally* UNE Loop Order. The evidence adduced in that proceeding is what is being considered here. The Commission authorized SBC to increase UNE loop rates, based upon SBC's assertion (concurred in, to a modest extent by the Staff) that SBC's costs of providing UNE loops increased since last being set. The UNE loop rates thus set – supported by a significant, not to say excruciating, amount of evidence – are now the basis for imputation tests in this proceeding. It is therefore quite impossible to thus suggest, as the IPTA does, that the UNE loop rates at issue here were somehow the subject of a lesser degree of evidentiary presentation and

[1] Indeed, "scores" of witnesses (and in any case, well in excess of twenty) offered testimony; in contrast, despite IPTA's hyperbolic assertions, it offered the testimony of *three* witnesses in the *Payphone Proceeding*.

Commission deliberation than the COPTS rates set in compliance with the *Payphone Order*. Staff RB at 59-60.

Staff, accordingly, concludes that the UNE loop costs used in this proceeding rest upon a strong evidentiary basis. IPTA cannot be heard to assert that the Commission would be acting in an arbitrary and capricious manner were it to require SBC to file new COPTS rates based on the costs developed in the UNE Loop proceeding. Staff RB at 60.

Staff pointed out that SBC's position is markedly clearer, and consistent with Staff's to some extent. Staff found SBC's characterization that COPTS rates are not, as the IPTA would have the Commission believe, "locked in concrete" to be a fair characterization of the state of the law. Staff RB at 61 (citations omitted).

Staff noted, however, that SBC departs from the Staff's position, and in fact from the *Payphone Order*, however, in its proposal that the "the direct cost basis for the [COPTS] rates be revisited." Staff noted that while SBC is correct in asserting that "the Commission[-]approved … LRSIC-based methodology … was not heavily litigated" this was chiefly because SBC filed a LRSIC study in support of its proposed rates, presumably because the LRSIC for the COPTS service was higher than (although not markedly different from) the TELRIC for the access line. Staff RB at 61 (citations omitted).

Staff pointed out that the fact remains that the Commission ordered the use of LRSIC in its *Payphone Order*. Payphone Order at 37. SBC's proposal to use TELRIC is therefore inconsistent with the Payphone *Order*. Moreover, SBC can presumably develop LRSIC studies for COPTS using its LoopCAT model, use of which, as noted above, the Commission has approved. Accordingly, the Staff is uncertain why SBC would wish to use TELRIC (as LRSIC is likely to be higher, at least to the extent developed using LoopCAT), other than ease of implementation. Staff RB at 61-62.

C. Rate Options If Preemption Does Not Apply

1. Direct Testimony

Mr. Koch did not address this issue in his direct testimony. See Staff Ex. 1.0.

2. Rebuttal Testimony

Mr. Koch did not address this issue in his rebuttal testimony. See Staff Ex. 2.0.

3. Legal Argument in Briefs

Staff pointed out that one solution that the Commission might consider is to order SBC to modify its retail COPTS rates. This appears to be a feasible approach. The Commission has, in the *Payphone Order*, set forth a methodology to set – and, accordingly, to reset – COPTS rates. As shown above, factors affecting this methodology have changed as a result of the SBC UNE Loop Order. Under this approach, SBC would file revised tariffs supported by an up-to-date LRSIC study, and using an up-to-date shared and common cost loading. SBC IB at 63-64.

In its Reply Brief, the Staff remains convinced, and continues to recommend, that there is no federal preemption issue here, that COPTS rates must pass imputation, that there is no impediment to the Commission ordering SBC to file revised LRSIC studies (modeled using LoopCAT) and using the new UNE Shared and Common Cost markup with new COPTS tariffs such as satisfy imputation. Staff RB at 62.

VII. Conclusion

Staff is convinced that SBC's retail business NAL is subject to imputation; that the UNE loop is a noncompetitive service or service element used to provide a competitive service within the meaning of Section 13-505.1 of the Public Utilities Act, such that SBC's retail business NAL must satisfy imputation based upon the TELRIC rate it charges for the UNE loop. Staff is further convinced that a "narrow" imputation test is the only lawful and proper test to use, and that revenues from usage and vertical services cannot and should not be included. Staff contends that SBC's retail business NAL rates do not pass imputation under a properly constructed test. Staff notes that there a number of rate design options that SBC can use to deal with this problem, but the Commission is under no obligation to give SBC direction or guidance in this regard. Finally, the Staff argues that Section 276 does not preempt the application of the imputation test to COPTS rates, and those rates can be altered consistent with both Section 276 and imputation, based on the methodology established by the Commission in its *Payphone Order*.